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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1985

ROBERT BOGGILD and WILLIAM L. DALE,
Petitioners,

v.

KENNER PRODUCTS, A DIVISION OF
CPG PRODUCTS CORPORATION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

I. Does a federal supremacy doctrine based on Article I, Section 8 of the Constitution require that a licensee be permitted to escape further payment of royalties by claiming *per se* invalidity of the license agreement beyond the expiration of a subsequently issued patent covering the subject matter of the license, where the royalties are based on trade secrets and technical services and the leverage of a potential patent monopoly did not influence the making of the agreement?

II. In reviewing the granting of summary judgment for the licensor, may the Court of Appeals make findings of fact concerning the parties' use of the leverage of a potential patent, and thereupon hold the agreement "*per se*" invalid beyond the expiration of such a patent?

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

Petitioners respectfully request that a Writ of Certiorari be issued to review the decision and judgment of the United States Court of Appeals for the Sixth Circuit entered on November 13, 1985, which reversed the decision of the United States District Court for the Southern District of Ohio, Western Division, granting summary judgment in favor of the Petitioners.

OPINIONS BELOW

The opinion of the Court of Appeals is contained in the Appendix at 1a, and is reported at 776 F.2d 1315. The opinion of the District Court granting summary judgment is contained in the Appendix at 12a, and is reported at 576 F. Supp. 533.

JURISDICTION

The judgment of the Court of Appeals was entered on November 13, 1985. A Petition for Rehearing was timely filed by the Petitioners on November 26, 1985. The Petition for Rehearing was overruled on January 2, 1986. Jurisdiction to review the judgment of the Sixth Circuit in this cause by a Writ of Certiorari is conferred on this Court by 28 U.S. Code § 1254(1).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Article I, Section 8, U.S. Constitution:

> "The Congress shall have Power . . . To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their repective Writings and Discoveries;"

35 U.S.C., Section 154:

> "Every patent shall contain a short title of the invention and a grant to the patentee, his heirs or assigns, for the term of seventeen years, subject to the payment of fees as provided for in this title [35 USCS §§ 1 et seq.], of the right to exclude others from making, using, or selling the invention throughout the United States, referring to the specification for the particulars thereof. A copy of the specification and drawings shall be annexed to the patent and be a part thereof."

STATEMENT OF THE CASE

The Petitioners are the inventors of a toy extrusion device designed to be used with the modeling compound Play-Doh. On January 18, 1963, the Petitioners entered into a trade secret licensing agreement with Kutol Products, Inc., which at that time was manufacturing Play-Doh. The Respondent, Kenner Products, a Division of CPG Products Corp. (hereinafter "Kenner"), is the successor-in-interest to the rights and liabilities of Kutol Products, Inc. under the said trade secret licensing agreement. CPG Products Corp. is a Delaware corporation whose principal place of business is in Minnesota. Kenner has its offices and some of its manufacturing facilities in Cincinnati, Ohio.

This action was commenced in the Common Pleas Court of Hamilton County, Ohio, on March 24, 1983. In their complaint in the state court, Petitioners alleged in substance that Kenner had shortchanged the Petitioners on royalty payments since it had first begun marketing Petitioners' extrusion device in 1971, by making certain unilateral, unauthorized deductions from the sale price of the extruder before applying Petitioners' royalty rate of 5%.

In response to the state court complaint, Kenner petitioned for removal of the action from the state court to the United States District Court for the Southern District of Ohio, Western Division, at Cincinnati. The basis asserted by Kenner for federal jurisdiction was diversity of citizenship, 28 U.S.C. § 1332. Upon removal of the action to the District Court, Kenner filed an Answer and Counterclaim in which it asserted, as its eighth affirmative defense and its second counterclaim, the contention that as of August 9, 1983, the date of expiration of the last-to-expire patent on the extrusion device, Kenner would be free of the obligation to pay royalties under the License Agreement, even though the agreement, by its terms, would not expire until January 18, 1988. Petitioners moved for judgment on the pleadings with respect to the sufficiency of Kenner's eighth affirmative defense and second counterclaim; and Kenner in turn moved

for summary judgment, asserting that it was entitled to judgment as a matter of law on that defense and counterclaim.

On December 15, 1983, the District court issued its opinion and order sustaining Petitioner's motion and overruling the motion of Kenner. The District Court refused to certify its December 15, 1983 ruling for immediate appeal, under either rule 54(b) Federal Rules of Civil Procedure, or 28 U.S.C. § 1292(b). Thereafter, a settlement was reached between Kenner and the Petitioners with respect to the claims for past underpayment of royalties, and a consent decree was entered into, which was placed of record on June 12, 1984. Among other things, the consent decree certified the December 1983 ruling as final and appealable.

From that judgment, Kenner took its appeal to the United States Court of Appeals for the Sixth Circuit by Notice of Appeal filed on June 15, 1984. After briefing and argument, the Court of Appeals rendered its opinion and judgment on November 13, 1985, reversing the order of the District Court granting partial summary judgment for the Petitioners and remanding "for proceedings consistent with this opinion." In its opinion, the Sixth Circuit also reviewed the subject licensing agreement in the light of its interpretation of *Brulotte* v. *Thys Co.*, 379 U.S. 29, 85 S.Ct. 176 (1964), and held that the agreement was unlawful *per se* beyond the expiration dates of the patents. A timely Petition for Rehearing was denied on January 2, 1986.

In the late 1950's and early 1960's, Joseph McVicker, the owner of Kutol Products, Inc., who had been making and marketing a brand of wallpaper cleaner, decided that his product would also make a good modeling compound. He began to make his compound in a number of bright colors, with a more pleasant scent, and called it Play-Doh. The trouble with marketing a modeling compound was that whether it was Play-Doh or clay, most children soon tired of playing with it, unless they had some artistic talent, because most children did not have the ability or the imagination to create interesting or exciting shapes with it.

In order to make Play-Doh more marketable, McVicker

turned to Boggild and Dale, who agreed to submit designs for a number of simple devices by which children could turn Play-Doh into unusual and interesting shapes and forms. One of the first, and certainly the most successful, of the devices which Boggild and Dale invented for McVicker and Kutol Products, Inc. was the Play-Doh extruder marketed under the name "Fun Factory, Jr." A copy of a pictorial representation of the extruder is provided in the Appendix to this Petition, page 55a.

The trade-secret License Agreement between Boggild and Dale as licensors and Kutol Products, Inc. as licensee (Appendix, pp. 27a-38a) was a comprehensive document. Not only did it grant to Kutol the right to make, use, and sell the extrusion device as designed by Boggild and Dale and disclosed to McVicker, but it also provided that Boggild and Dale would:

(1) Provide engineering drawings (Article V); (2) Provide working models for demonstration to potential customers (Article V); (3) Participate in negotiations to obtain suppliers for parts (Article V); (4) Work with parts manufacturers and/or assemblers until the product was established in satisfactory repetitive manufacture (Article V); (5) Redesign the device to eliminate any design or mechanical faults (Article V); (6) Establish the standards for manufacture of the device (Article V); (7) Communicate technical know-how, data or other information pertinent to the extrusion device at that time in Petitioners' possession or "which may hereafter within the term of this Agreement be acquired by B and D" (Article V); (8) Cause a patent infringement search to be made (Article XIV); (9) submit an opinion regarding the likelihood of infringement (Article XIV); (10) File mechanical and design patent applications (Article II).

At the time that the License Agreement was negotiated and entered into, there was no patent application pending. There was in the agreement no requirement for an opinion of counsel concerning the likelihood that any patents would issue. While the agreement required Petitioners to file and prosecute patent applications, the royalty terms of the agreement were expressly made independent of whether or not the

extrusion device was patentable. Thus, Article VI(f)(1) of the License Agreement provided that the royalty rate would escalate from 3% to 4% to 5% on the basis of the number of units of the extruder sold by the licensee—not on the basis of whether any patent was issued. Once 500,000 units were sold, the royalty rate was to be 5%. Article VI(g) of the License Agreement provided that the payment of such royalties was to continue

> "regardless of whether or not the filing of the patent applications contemplated in Article II hereof results in the issuance of a patent or patents."

In return for the assignment of rights and the other benefits and considerations agreed upon and described above Kutol Products, Inc. agreed to pay Boggild and Dale royalties for a period

> "which shall run to the full end of the term or terms of any Letters Patent that may issue on or as a result of the application or applications referred to in Article II hereof, or for a period of 25 years, whichever is longer, and shall thereupon terminate" (Article XIII(d)).

The term of the License Agreement thus did not *necessarily* extend for a period beyond the life of any patents which might issue. At the time the agreement was negotiated, it was not unlikely that the patent application contemplated in Article II could be pending for eight years or more before any patent was issued, with the result that the minimum 25 year term of the agreement would be shorter than the patent lives. (Play-Doh itself had taken nine years to receive a patent.)

As agreed, the Petitioners filed mechanical and design patent applications, which resulted in the issuance of Design Patent No. 200,480 on March 2, 1965, and Mechanical Patent No. 3,264,685 on August 9, 1966.

Joseph McVicker was not influenced in his negotiation of the royalty terms of the licensing Agreement by the expectation that any patents would issue. In his deposition taken in California on December 19, 1985,[1] Mr. McVicker testified that the likelihood that the device would be patented did not affect his willingness to pay royalties for a term of at least 25 years:

> Q: Did the thought that this device may be patentable influence in any way, your desire to pay royalties for the use of the device and to pay those royalties for that period of time?
>
> A: The patent and the application and the assertion of the patent, and the possible issuance of a patent, did not determine my making a deal with Boggild. What determined it was a whole package, which included their giving me technical and manufacturing assistance, solving manufacturing problems, taking responsibility to search infringement, the cost of filing for an application and seeing it through without any cost or liability to me; and that's the deal I made with them. (McVicker Deposition, p. 12)
>
> * * *
>
> Q: The agreement contained certain provisions with respect to patent and patent applications. Given that, can you tell us what, if any, role the expecta-

[1] When it became apparent upon the issuance of the Sixth Circuit's opinion that an issue of fact concerning the parties' "expectations that a valid patent will issue" may be dispositive of the case, permission was obtained from the District Court under Rule 27(b) Federal Rules of Civil Procedure, to take Mr. McVicker's deposition. A copy of that deposition appears on pages 39 through 54 of the Appendix of this Petition.

tion that a patent might issue for this device played in your willingness to pay royalties for the use of the device?

A: That's a long question. Please rephrase it simply for me.

Q: Let me try Did the likelihood that this device would be patented affect your desire to pay royalties for it?

A: No, I couldn't wait for that. The patent process is lengthy, and, I think, fairly worthless. It took me nine years to get a patent on Play-Doh. I don't know how long it took to get a Fun Factory, Jr. patent, but if I waited for that, someone else may have invented a toy to take its place. . . .

* * *

Q: When did you have—did you have any idea when you signed that agreement, that this toy was going to be patented?

A: I don't know, but I certainly asked, after this bad experience that I had if I would be protected any way I could be protected, and they should at least see if they could get a patent protection, and protection is an additive, but it is not determinative for me. What determines it is, can I sell it and can I get it to the market first? (McVicker Deposition, pp. 10-11)

ARGUMENT

I. REASONS FOR ALLOWANCE OF THE WRIT OF CERTIORARI.

This is a clear-cut case of a licensee cloaking itself in the mantle of the public's interest in the free exploitation of ideas in order to escape having to pay royalties on a license agreement its predecesssor freely bargained for. This masquerade is possible only because the Circuit Courts have failed to analyze and properly apply this Court's holdings in *Brulotte* v. *Thys Co.*, 379 U.S. 29, 85 S.Ct. 176 (1964), and *Aronson* v. *Quick Point Pencil Co.*, 440 U.S. 257, 99 S.Ct. 1096 (1979), and because this Court has so far not seen fit to set them straight—presumably because the right case hasn't yet come along.

This is the right case. Kenner products, the corporate successor to the market-savvy entrepreneur Joe McVicker, has for years reaped profits from the market position established by McVicker for Play-Doh and for the toy extrusion device invented by the Petitioners. The subject trade-secret license agreement enabled McVicker to be first in the marketplace with the extruder, whose marriage with Play-Doh produced millions of sales. In return for this opportunity, and for the technical services of the Petitioners in starting up and continuing production, McVicker agreed to pay the Petitioners royalties for a minimum term of 25 years—regardless of whether or not the extruder was patentable.

The agreement required patent applications to be made, however, and patents were issued. Taking its cue from the *"per se"* language of *Brulotte* and from certain *dicta* by this Court in *Aronson*, Kenner says the expiration of those patents excuses it from paying further royalties.

The District Court looked behind the *"per se"* language of *Brulotte* and saw that it couldn't be applied to an agreement made when no patent existed or was even applied for. The Sixth Circuit Court of Appeals, following the Eleventh Circuit in *Pitney Bowes* v. *Mestre*, 701 F.2d 1365 (11th Cir. 1983), *cert. den.* 104 S.Ct. 239 (1983), tried to apply a *per se*

rule, but ended up making findings of fact on whether the Petitioners used the leverage of a potential patent monopoly to negotiate the royalty term.

The law in this important area of intellectual property licensing is now in a state of confusion which only this Court can correct. *Brulotte* and *Aronson*, together with *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 94 S.Ct. 1879 (1974), clearly mean that a trade secret license agreement can be invalidated only if the leverage of a patent monopoly is used to extend royalty payments for patented subject matter beyond the life of applicable patents. Only then is there a conflict between state and federal law. But this leverage issue is a question of fact, not a *per se* issue of law. As the Circuit Courts are applying *Brulotte*, however, the mere presence of a patent, covering the subject matter of a license agreement, no matter how inconsequential it is to the bargain, may be used to destroy the bargain after the fact. For example, if for the sake of completeness the parties decide to recite a patent in an agreement covering trade secrets, and that patent has but three months left in its term, the Sixth Circuit's application of a *per se* rule of invalidity would require that the license agreement expire in three months, contrary to the wishes of the parties, simply because the patent is there.

Such results artifically restrict the ability of inventors and licensees to bargain freely the value of inventions in the marketplace. Inventors are also thereby discouraged from applying for patents, if the patent can be used to limit royalties which the free market for new ideas will otherwise bear.

This case presents to the Court for the first time a clear-cut set of facts upon which the Court can dispel the confusion and settle, once and for all, the issue of what circumstances require an agreement to pay royalties to be voided by overriding public policy inherent in the patent laws. This case contains the following elements which have not been present in any prior case this Court has had the opportunity to review:

(1) No pending patent application at the time the agreement was made;

(2) Patent issuance and expiration during the term of the agreement;

(3) Substantial technical services rendered by the licensors in addition to the licensing of the invention; and

(4) Affirmation, both in the terms of the agreement and in available testimony, that the parties assigned no value, in terms of royalties, to the potential issuance of a patent covering the invention.

The Sixth Circuit's attempted application of a *per se* rule of invalidity was inappropriate here and in conflict with this Court's reasoning in *Brulotte*, *Kewanee*, and *Aronson*, as noted above and as more fully discussed below.

In addition, the Sixth Circuit clearly departed from the accepted and normal course of judicial proceedings by making findings of fact on the patent-leverage question, and thereupon purporting to find the agreement unlawful "*per se.*"

The confusion inherent in the Sixth Circuit's decision may indeed have put this case into an unreviewable posture at this time. Since there are no findings of fact by the proper trier of the facts on the issue of patent leverage, the appropriate disposition of the case may be to remand it for trial, by summary disposition under Rule 23.

II. FIRST QUESTION PRESENTED FOR REVIEW.

Does a federal supremacy doctrine based on Article I, Section 8 of the Constitution require that a licensee be permitted to escape further payment of royalties by claiming per se invalidity of the license agreement beyond the expiration of a subsequently issued patent covering the subject matter of the license, where the royalties are based on trade secrets and technical services and the leverage of a potential patent monopoly did not influence the making of the agreement?

Disposition of this case depends, in the first instance, on the interpretation of *Brulotte* v. *Thys Co.*, *supra*, and its "*per se*" language. In *Brulotte*, the owner of various patents for hop picking sold machines incorporating the patents for flat sums, and issued licenses for the use of the patents as incorporated into the machines, requiring the payment of royalties for the licenses over and above the purchase price of the machines. The contracts in issue were negotiated either during the life of the patents involved or following the expiration of some of them. None of the contracts were negotiated prior to issuance of or application for patents. The contracts provided for the payment of royalties beyond the expiration dates of the patents.

With patents in effect when the *Brulotte* agreements were made, it seems to have appeared to this Court that any projection of the obligation to pay royalties was "a tell-tale sign that the licensor was using the licenses to project its monopoly beyond the patent period." 85 S.Ct. at p. 179. Under those circumstances, this Court found itself "unable to conjecture what the bargaining position of the parties might have been and what resultant arrangement might have emerged had the provision for postexpiration royalties been divorced from the patent and *nowise subject to its leverage.*" 379 U.S., at 32; 85 S.Ct. at 179, emphasis supplied. Clearly, it is the use of the patent monopoly to leverage an obligation to pay royalties beyond the patent's monopoly period, which this Court found

unlawful in *Brulotte*. In that case, because the patents were in effect at the time the license agreements were negotiated, it may have been difficult to conceive of the negotiations being conducted without the leverage of the patent monopoly having an influence. Therefore, this Court concluded "that a *patentee's* use of a royalty agreement that projects beyond the expiration date of the patent is unlawful *per se*." 379 U.S., at 32; 85 S.Ct. at 179, emphasis supplied.

The "*per se*" rule of *Brulotte* is thus limited to the case presented there, where the owner of existing patents uses the leverage of the patent monopoly to project royalty payments beyond the life of the patents. Where the patents are in existence at the time of negotiations, the influence of their leverage upon negotiations may be rebuttably presumed.

But it is clear that what renders an agreement invalid under the *Brulotte* rule is the leveraging of the patent monopoly to exact royalties beyond the expiration date of the patent; not simply the fact that the royalty obligation under the agreement continues after patents expire. Thus, this Court said in *Brulotte:*

> "A patent empowers the owner to exact royalties as high as he can negotiate with the leverage of that monopoly. But *to use that leverage to project those royalty payments beyond the life of the patent* is analogous to enlarging the monopoly of the patent by tying the sale or use of the patented article to the purchase or use of unpatented ones." (379 U.S. at 33; 85 S.Ct. at 179 (emphasis supplied).)

Where there are no issued patents at the time of negotiations, but only a pending patent application or a promise to apply for a patent, it is evident that something other than a potential patent monopoly may influence the parties to enter into the License Agreement. It is probable that in most cases, as in the present case, that influence is the desire of the licensee to obtain the right to be the first in the marketplace to exploit the novelty of the licensed invention. In such a case,

the parties to the agreement may or may not be influenced in their negotiations by the expectation that a patent will issue. There can therefore be no *per se* presumption of invalidity simply because royalty payments may be provided to extend beyond the expiration date of patents which may later issue. The District Court recognized this fact in its decision as follows:

> "We recognize that, regardless of whether an application has been made, one might improperly leverage the possibility that the patent might issue if the parties believe there is a substantial likelihood that a patent might issue. Under those circumstances, however, application of a *per se* rule is inappropriate. We hold therefore, that the *per se* rule of *Brulotte* does not extend to the case where no patent application has been made at the time the agreement is negotiated even if an application is contemplated." 576 F. Supp. at 536-537.

This Court also recognized the limitation of the *per se* rule of *Brulotte* in the opinion of the Court in *Aronson* v. *Quick Point Pencil Co.*, 440 U.S. 257, 99 S.Ct. 1096 (1979). In that case, a trade secret license for a simple, novel, keyholder device was negotiated while a patent application for the device was pending. Unlike the present case, no patent was later issued for the device, and the agreement provided for a reduced royalty in the event that a patent did not issue. This Court held the *Aronson* agreement to be enforceable, holding first that the enforcement of the agreement did not present a conflict with federal patent law, and second, that enforcement of the royalty agreement was "consistent with the principles treated in *Brulotte* v. *Thys Co.*":

> "There, we held that the obligation to pay royalties in return for the use of a patented device may not extend beyond the life of the patent. The principle underlying that holding was simply that the monopoly granted *under a patent* cannot lawfully be used to 'negotiate

> with the leverage of that monopoly'." 440 U.S. at 264-65; 99 S.Ct. at 1100 (emphasis by the Court).

With respect to the leverage afforded by a potential patent, this Court noted in *Aronson:*

> "No doubt a pending patent application gives the applicant some additional bargaining power for purposes of negotiating a royalty agreement. The pending application allows the inventor to hold out the hope of an exclusive right to exploit the idea, as well as the threat that the other party will be prevented from using the idea for 17 years. *However, the amount of leverage arising from a patent application depends on how likely the parties consider it to be that a valid patent will issue.* 440 U.S. at 265, 99 S.Ct. at 1100-101 (emphasis supplied).

This language of the Chief Justice's opinion is wholly inconsistent with any notion that a trade secret licensing agreement negotiated with a patent application pending can be unlawful *per se* just because it may extend beyond the life of a patent which might later issue. *A fortiori*, there can be no *per se* invalidity where, at the time of negotiations, no patent has even been applied for and no infringement search has been undertaken, even though the parties contemplate the doing of both. Plainly, the leverage of a *potential* patent monopoly must be *proven* to have influenced the royalty term of the agreement, in order for the *Brulotte* rule to invalidate it. In such case, however, the agreement is not invalid *per se:* it is invalid only to the extent of the leverage exerted by the potential patent monopoly.

Underlying the *Brulotte* rule is the principle that trade secret licensing agreements may not be enforced to the extent that they conflict with the policies and purposes of federal patent law. Although detailed discussion and explication of this conflict issue did not appear in the *Brulotte* opinion, but was left to later decisions of this Court in *Kewanee Oil Co.* v. *Bicron Corp.* 416 U.S. 270, 94 S.Ct. 1879 (1974), and *Aron-*

son v. *Quick Point Pencil Co.*, *supra*, it is clear that an instance of such conflict occurs where a patentee uses the leverage of his patent to negotiate a licensing agreement which provides for the payment of royalties after the expiration of the patent, and the patentee seeks to enforce the extended royalty obligation by invoking state contract law.

It is *the leveraging of the patent monopoly* to extend the royalty payments which sets up the conflict. As this Court noted in *Kewanee* and *Aronson*, there is no conflict between state trade secret licensing law and federal patent law *per se*. Trade secret licensing law and patent law, by this Court's analysis in those cases, can coexist in the same agreement, so long as the state law does not interfere with the objectives of the patent law. (*See*, *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. at pp. 479-80; and *Aronson* v. *Quick Point Pencil Co.*, 440 U.S. at pp. 262-63, 99 S.Ct. at pp. 1099-1100.) The District Court followed this Court's analysis and determined that enforcement of the existing licensing agreement did not *per se* present a conflict between state law and federal patent law and policy, even though, in this case, patents did issue. 576 F. Supp. at 537-39. The Sixth Circuit, however, in its opinion in this case, failed to address that analysis.

In *Pitney Bowes* v. *Mestre*, 701 F. 2d 1365 (11th Cir. 1983) *cert den.*, 104 S.Ct. 239, the Eleventh Circuit seemed to recognize that even though a patent issues after a license agreement is entered into, the issuance of the patent does not itself set up a conflict between patent law and trade secret law; rather, "when a patent issues, the *potential* exists for direct conflict between federal patent law and state trade secret law." 701 F.2d at 1372, emphasis supplied. In footnote 12 of the Eleventh Circuit's opinion in *Mestre*, 701 F.2d at 1372-73, the Court noted that it is the improper use of the patent monopoly leverage which sets up the conflict in such a case:

> "This does not mean that parties cannot agree to license both trade secrets and patent rights *on patents actually issued*. As the Court in *Kewanee* noted, the purposes of

> patent protection and trade secret protection usually are entirely different, and the enforcement of trade secrets need not necessarily undermine federal patent policy, (citations omitted) but *if and when their purposes conflict directly*, federal supremacy requires that federal patent law determine the rights under the agreement." (Emphasis supplied.)

In concluding that footnote, the Eleventh Circuit recognized that even where a patent issues, there may be no conflict between trade secret law and patent law if it can be shown that the leverage of a patent monopoly was not used to exact trade secret royalty payments beyond the life of the patent:

> Indeed, the Supreme Court has never addressed the question whether a hybrid agreement in which patents issue can ever survive the expiration of the patents. The Court in *Brulotte*, however, applied a *per se* rule to agreements containing the same terms before and after the patent expires because it was 'unable to conjecture what the bargaining position of the parties might have been' had no patent been involved. 379 U.S., at 32, 85 S.Ct., at 179. The implication of this language is that, if a patent owner can prove that he did not use his patent monopoly leverage to exact reduced post-expiration trade secret payments, then there would be no direct conflict with federal law and the agreement would be enforced." 701 F.2d at 1373, n. 12.

Both the Eleventh Circuit in *Mestre* and the Sixth Circuit in this case emphasized the fact that in *Aronson*, no patent had issued, and relied upon certain *dicta* in this Court's *Aronson* opinion as an indication of what this Court's opinion would be if, as in the present case, it were faced with a fact situation which included the issuance of a patent during the term of the licensing agreement. See, *Mestre*, 701 F.2d, at p. 1372; and *Boggild*, 776 F.2d, at p. 1319-1320, footnote 5. The full quotation of this Court's *dicta* appears in *Aronson*, 440 U.S. at 263-64, 99 S.Ct. at 1100:

> "Finally, enforcement of this agreement does not discourage anyone from seeking a patent. Mrs. Aronson attempted to obtain a patent for over five years. It is quite true that had she succeeded, she would have received a 5% royalty only on keyholders sold during the seventeen year life of the patent. Offsetting the limited terms of royalty payments, she would have received twice as much per dollar of Quick Point's sales, and both she and Quick Point could have licensed any others who produced the same keyholder. Which course would have produced the greater yield to the contracting party is a matter of speculation; the parties resolved the uncertainties by their bargain."

These *dicta* do not necessarily indicate that this Court would hold that the issuance of a patent precludes the enforcement of a trade secret licensing agreement beyond the life of the patent, even where no leverage of an actual or potential patent monopoly was used to negotiate the royalty term. These *dicta* may equally well be read to comment on the effect of the terms of the contract. Thus, the agreement provided that Mrs. Aronson would receive a 5% royalty only if the licensed device were patented; otherwise, she would receive a reduced royalty of 2½%. The 5% royalty would be clearly contingent upon the attaining and licensing of patent rights, and therefore it could only be effective during the 17-year life of a patent. Similarly, the 2½% reduced royalty would only be payable, under the terms of the agreement, if a patent had not issued. The parties could have provided for the reduced royalty to continue after the expiration of the patent, without setting up a conflict with patent law. As this Court noted, the reduced royalty clearly was not negotiated with the leverage of a patent:

> "It is clear that whatever role the pending application played in the negotiation of the 5% royalty, it played no part in the contract to pay the 2-½% royalty indefinitely." 440 U.S. at 265, 99 S.Ct. at 1101).

If it is lawful to negotiate a reduced royalty to be applied after the expiration of a patent, clearly the issuance of the patent does not *ipso facto* establish such a conflict between the trade secret license and the patent so as to render the former invalid and unenforceable after the patent expires. If acceptance of this case for review accomplishes nothing else, presumably it will at least obviate the further necessity of speculating on the basis of *dicta* what this Court's decision would have been if a patent had issued in *Aronson*.

In *Brulotte*, applicability of the same royalty provisions before and after expiration of the patents was viewed by this Court as "a tell-tale sign that the licensor was using the license to project its monopoly beyond the patents." 379 U.S. at 32, 85 S.Ct. at 179. In *Mestre* and in the present case, the courts of appeals relied on the lack of difference in royalties before and after patent expiration as a sort of "rule of thumb" indicating invalidity of the agreement.

Evidently, in *Mestre* there was no evidence as to whether or not the pending patent applications provided leverage to influence the original licensee to agree to pay royalties for a period beyond the life of the patents. (In the present case, as the Statement of Facts reveals, such evidence is available.) Without such evidence, the Eleventh Circuit, noting no apparent allocation between patent royalties and nonpatent royalties on the face of the agreement, applied the "rule of thumb" and held the agreement invalid. In the present case, the Court of Appeals specifically relied upon the lack of allocation of royalties as an indication of improper leveraging of the patent monopoly. *See*, 776 F.2d at p. 1319.

But the key to the analysis, again, is not the *amount* of the post-expiration royalty payment, but whether the leverage of a potential patent monopoly influenced the licensee's willingness to pay that amount. Thus, in *Mestre* the Eleventh Circuit observed:

"Assuming that the value of the agreement to Pitney

> Bowes was not as high after the patents expired, it is reasonable to assume that at least some part of the post-expiration payment constituted an effort to extend payments for patent rights beyond the patent period." 701 F.2d at p. 1373.

Such assumptions are valid only in the absence of evidence to the contrary. What if it could be shown that the value of the agreement to the licensee was the same with or without patent protection? Article VI(g) of the agreement in the present case provided that the same royalties would be paid "regardless of whether or not the filing of patent applications contemplated in Article II hereof results in the issuance of a patent or patents." That provision is most appropriately viewed as a clear expression of the intent and understanding of the parties that the patentability of the extruder was immaterial to the willingness of the licensee to pay royalties. Indeed, the available evidence shows that in this case, as in *Aronson*, the primary value of the license was to enable the licensee to be first in the marketplace with a novel idea. The parties assigned a zero value to the patents.[2]

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[2] Another matter of allocation may be pertinent. It should be noted that in the present case, the licensing agreement required the licensors to provide a great deal of technical know-how and actual technical services in preparing the extrusion device for mass production. (Article V.) As the McVicker deposition reveals, Mr. McVicker left it entirely up to Boggild and Dale to handle the engineering of the extruder, for all of which work they would be compensated only through the medium of the royalty, while McVicker handled the marketing of the product. (McVicker Deposition, p. 6; Appendix, p. 43a.) There is substantial authority for the proposition that even if royalties for *rights* may not be payable under an agreement because a patent has expired or has been declared invalid, nevertheless, royalties for "nonpatent assets," such as engineering know-how, may remain payable and enforceable. See, e.g., *Chromalloy American Corp.* v. *Fischmann*, 716 F.2d 683 (9th Cir. 1983); *Span-Deck, Inc.* v. *Fab-Con, Inc.*, 677 F.2d 1237 (8th Cir. 1982), *cert. den.*, 103 S.Ct. 318 (1982); *St. Regis Paper Co.* v. *Royal Industries*, 552 F.2d 309 (9th Cir. 1977), *cert. den.*, 98 S.Ct. 633 (1977).

Petitioners respectfully suggest that *Brulotte* and *Mestre* are the beginning, not the end of this inquiry. In order to do justice among parties who have freely and fairly negotiated a trade secret licensing agreement which happens to outlive a subsequently issued patent, and in order to prevent a licensee from unjustly evading the royalty obligation it or its predecessor freely assumed, a searching inquiry must be made on the issue of leverage.

(Footnote 2 Continued)—

Remand of this case for trial will permit not only the reception of evidence on the "leverage" issue, but also on the issue of allocation of royalties between patent rights and nonpatent technical services and know-how. At the very least, the fact that the royalties in question were the sole compensation for the technical services and know-how to be rendered further diminishes the notion that the parties to the present agreement were influenced in their royalty negotiations by the possibility that a patent might later issue.

III. SECOND QUESTION PRESENTED FOR REVIEW

In reviewing the granting of summary judgment for the licensor, may the Court of Appeals make findings of fact concerning the parties' use of the leverage of a potential patent, and thereupon hold the agreement "*per se*" invalid beyond the expiration of such a patent?

As noted above, the District Court held that the application of a *per se* rule of invalidity was not appropriate where at the time of negotiation of the licensing agreement no patent had been issued or applied for.

> "We recognize that, regardless of whether an application has been made, one might improperly leverage the possibility that a patent might issue if the parties believe there is a substantial likelihood that a patent might issue. Under those circumstances, however, application of a *per se* rule is inappropriate. We hold, therefore, that the *per se* rule of *Brulotte* does not extend to the case where no patent application has been made at the time the agreement is negotiated even if an application is contemplated." 576 F. Supp. at 536-37.

Later in its opinion, after thoroughly considering the issue of conflict between trade secret licensing law and patent law in the light of this Court's decisions in *Kewanee* and *Aronson*, the District Court recognized that it still had to resolve the question of whether the Plaintiffs had used the leverage of a potential patent monopoly to extend the royalty payments beyond the lives of the patents. The District Court found that such leverage had not been used:

> "The answer to this question is located in the fact that the agreement at issue is one for the payment of royalties. Plaintiffs are not invoking the indeterminate protection of Ohio trade secret law. They are not seeking to prevent the public from manufacturing, selling, or using this invention. Rather, they seek to enforce the

> bargain they negotiated with defendant, i.e., the payment of royalties for a specified period in exchange for defendant's having the advantage of being first in the marketplace. We also note it was defendant—rather than plaintiffs—who primarily benefitted from the protection of the federal patent law. *We conclude, therefore, that plaintiffs did not use this agreement to extend their patent monopoly beyond the terms of the patents.* 576 F. Supp. at 539 (emphasis supplied).

The Court of Appeals disagreed with the District Court, and held that the *Brulotte* rule can be applied to invalidate *per se* a license agreement, such as the present one, where no patent was in existence or even applied for when the agreement was made:

> "We reverse this judgment and hold that the *Brulotte* rule of *per se* invalidity precludes enforcement of license provisions which were developed in anticipation of patent protection and which require royalty payments for use, sale or manufacture of a patented item beyond the life of the patent." 776 F.2d at 1319.

The Court of Appeals could not avoid, however, recognizing the fact that such a determination of "*per se*" invalidity depended upon the preliminary question of the use of patent leverage. Thus, in the first paragraph of its opinion, the Court of Appeals said:

> "We hold that under the rule of *per se* invalidity as established by *Brulotte* v. *Thys Co.* (citations omitted), the terms of a licensing agreement calling for royalty payments beyond the life of the patent are unenforceable *where the parties enter the agreement with clear expectations that a valid patent will issue.*" 776 F.2d at 1316 (emphasis supplied).

Indeed, the Court of Appeals cited and quoted this Court's statement of the leverage issue from *Aronson* as defining "the

nature of the leverage and the inquiry upon examination for abuse":

> "No doubt a pending patent application gives the applicant some additional bargaining power for purposes of negotiating a royalty agreement . . . However, the amount of leverage arising from a patent application depends on how likely the parties consider it to be that a valid patent will issue." 440 U.S. at 265, 99 S.Ct. at 1100, quoted at 776 F.2d, 1320.

Thus, both the District Court and the Court of Appeals recognized the preliminary issue that must be resolved before a *Brulotte* finding of invalidity can be made in the case of a licensing agreement negotiated before the issuance of a patent; and they each decided that issue differently. *That conflict alone demonstrates the existence of an issue of material fact.* The second issue which is presented to this Court, therefore, is whether the Court of Appeals properly decided the preliminary leverage question, or whether it should have remanded that question to the District Court for determination upon the reception of evidence on the question of whether "the parties enter(ed) the agreement with clear expectations that a valid patent (would) issue." 776 F.2d, at 1316. Curiously, the Court of Appeals reversed and remanded "for proceedings consistent with this opinion" *Id.*; and then went on to decide the issue of leverage, leaving the District Court nothing to do in such "proceedings."[3]

In this Court's formulation, as well as in that adopted by the Court of Appeals, the issue of leverage is a matter of the expectations, anticipations, and intentions of the parties to the licensing agreement at the time it was negotiated and

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[3] As noted above in the Statement of the Case, appeal was taken by Kenner only from the District Court's decision on the Eighth Affirmative Defense and Second Counterclaim, involving the claimed invalidity of the license agreement beyond the expiration date of the last patent. All remaining issues, primarily involving the method of calculating royalties, were resolved by a consent decree which was entered on June 12, 1984, and which was in the record before the Court of Appeals.

entered into. Such issues clearly are questions of fact. In *Pullman-Standard* v. *Swint*, 456 U.S. 273, 102 S.Ct. 1781, 72 L.Ed. 2d 66 (1982), this Court held that issues of intent are "factual matters for the triers of fact." 456 U.S. at 288, 72 L.Ed. 2d at 79. In the *Swint* case, the issue was whether a union seniority system had been adopted and maintained with discriminatory intent. After a lengthy trial, the District Court found that the seniority system was adopted and maintained wholly independent of any discriminatory intent. On appeal, the Court of Appeals for the Fifth Circuit reversed, reviewing the evidence and making its own finding of fact and invalidating the seniority system because it "resulted from an intent to discriminate because of race." (Quoted at 456 U.S. at 284, 72 L.Ed. 2d at 77.)

This Court reversed and remanded to the Court of Appeals for further proceedings, holding that the Court of Appeals had departed from the accepted and usual course of judicial proceedings by making findings of fact:

> "When an appellate court discerns that a district court has failed to make a finding because of an erroneous view of the law, the usual rule is that there should be a remand for further proceedings to permit the trial court to make the missing findings:
>
> > '[F]act finding is the basic responsibility of district courts, rather than appellate courts, and . . . the Court of Appeals should not have resolved in the first instance this factual dispute which had not been considered by the District Court.' " *DeMarco* v. *United States*, 415 U.S. 449, 450, n. 39 L.Ed. 2d 501, 94 S.Ct. 1185 (1974)

456 U.S. at 291-92, 72 L.Ed. 2d at 81-82.

The findings of the Court of Appeals were clearly and uniquely findings of fact. Thus, in concluding its opinion, the Court of Appeals found "that the parties assumed a high likelihood that valid patents would issue;" and "at the time the parties executed the license, the Plaintiffs exerted con-

siderable leverage from the anticipated patents." In its footnote 6, noting that Article VI of the agreement required royalty payments whether patents issued or not, the Court said "in light of the parties' clear contemplation of successful patent applications, the disclaimed relevance of the patent in Article VI must be discounted." 776 F.2d at 1321.

The *Swint* case, of course, involved the propriety of a court of appeals making findings of fact in reviewing the findings of a district court after trial, under the "clearly erroneous" standard of FED. R. CIV. P. 52(a). The impropriety of an appellate court making findings of fact in the first instance is equally, if not more, fundamental to appellate review of decisions on motions for summary judgment. A host of cases in the Circuit Courts have held that the role of an appellate court reviewing a summary judgment is to apply the same test as that utilized by the trial court to grant the motion, i.e., to determine whether there are issues of fact to be tried. If such issues of fact are discerned by the appellate court, it may not make findings of fact on those issues, but must remand to the trial court for findings of fact upon the reception of evidence. *McPhee* v. *Oliver Tyrone Corp.*, 489 F.2d 718 (5th Cir. 1974); *Radobenko* v. *Automated Equipment Corp.*, 520 F.2d 540 (9th Cir. 1975); *Glenway Industries, Inc.* v. *Wheelabrator-Frye, Inc.*, 686 F.2d 415 (6th Cir. 1982); *Ed Houser Enterprises, Inc.* v. *General Motors Corp.*, 595 F.2d 366 (7th Cir. 1979); *United States* v. *Gammache*, 713 F.2d 588 (10th Cir. 1983); *Molitor* v. *American President Lines, Ltd.*, 343 F.2d 217 (9th Cir. 1965).

Indeed, it has been held where, as the case was presented to the District Court, it was not apparent that any genuine issue of material fact was involved, but as the case unfolded in the Court of Appeals, genuine issues of material fact were revealed; under those circumstances, the Court of Appeals should reverse and send the case back for trial on those issues. *Smith* v. *U.S.*, 362 F.2d 366 (9th Cir. 1966).

The Court of Appeals attempted to resolve the issues of fact

regarding the intentions of the parties to this agreement by looking at the terms of the licensing agreement itself. The findings the Court of Appeals made, however, were severely flawed. None of them was clearly warranted by the language of the agreement itself, and all of them required the Court to indulge in assumptions concerning the intentions and expectations of the parties. Thus, for example, the Court of Appeals said that Article XIV, "Patent Infringement Search," required the licensors to obtain a patent infringement search "in order to determine the likelihood of receiving a patent." 776 F.2d at 1321. On the contrary, that was clearly not the case, because Article XIV in its very terms says that the patent infringement search was "in order to determine whether the within described extrusion device in its manufacturing, using or selling would constitute an infringement on a previously issued patent" (Appendix, p. 36a): in other words, whether the marketing of the device, patented or not, would infringe upon existing patents. Even accepting the Court of Appeals' construction of this provision, however, an infringement search to determine the likelihood of receiving a patent would clearly indicate that at the time of negotiating the agreement, the parties were decidedly uncertain about the patentability of the device.

In another instance, the Court of Appeals pointed to the provision of Article X that Kenner will admit the validity of any "patent under which rights herein are granted" as indicating "the parties' anticipation and expectation of successful patent applications." 776 F.2d at 1320. The opposite is true, however. This provision indicates, if anything, the uncertainty of the licensors that their invention was patentable. *Lear, Inc.* v. *Adkins*, 395 U.S. 653, 89 S.Ct. 1902, 23 L.Ed. 2d 610 (1969). Similarly, Article XIII(c), which gives the licensee the right to terminate the license in the event of unlicensed competition which the parties are "unable or unwilling to prevent or restrain," indicates that the licensee was uncertain, at the time of negotiation, that the extrusion device would be patentable. Yet, the Court of Appeals found

that this provision "suggests the entire license was premised upon the issuance of patents." 776 F.2d at 1321.

CONCLUSION

Once before, in its decision in *Kewanee Oil Co.* v. *Bicron Corp.*, 478 F.2d 1074 (6th Cir. 1973), *rev'd*, 416 U.S. 270 (1974), the Sixth Circuit Court of Appeals held that an Ohio trade-secret agreement could not be judicially enforced because its subject matter was preempted by the federal patent laws. This Court, of course, corrected the Sixth Circuit's view, and held that there was no federal preemption of the field of trade-secret licensing. Now, the Sixth Circuit has again mounted an attack on Ohio trade-secret law, holding in effect that wherever there is a patent, it must be held to obliterate any trade secret agreement covering the same subject matter, regardless of whether the parties to the agreement ascribed any decisive importance to patent protection. The Sixth Circuit's application of a *per se* rule of invalidity to the subject agreement, even though no patent existed at the time the agreement was made, was in conflict with this Court's analysis in *Brulotte* and *Aronson* that a conflict between state trade-secret law and federal patent law must first be shown by the leveraging of the potential patent monopoly before such an agreement may be held invalid. Finally, the Court of Appeals clearly departed from the accepted and usual course of judicial proceedings by making findings of fact upon review of a summary judgment involving the patent-leverage issue, rather than remanding the case for trial on that issue of fact.

While Petitioners would welcome full review of this case by the Court, in view of the Sixth Circuit's failure to remand for trial on the leverage issue, summary disposition of this cause under Rule 23 by a remand for trial on that issue will correct the error of the Court of Appeals and provide a proper factual

record to which this Court's *Brulotte*, *Kewanee*, and *Aronson* rules may be applied.

Respectfuly submitted,

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No. 84-3467

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

ROBERT BOGGILD; WILLIAM L. DALE,
Plaintiffs-Appellees,
vs.
KENNER PRODUCTS, a Divison of CPG PRODUCTS CORP.,
Defendant-Appellant.

ON APPEAL from the United States District Court for the Southern District of Ohio.

Decided and Filed November 13, 1985

Before: KEITH and MARTIN, Circuit Judges; and DIGGS TAYLOR.*

KEITH, Circuit Judge: The issue in this case is whether the terms of a licensing agreement, which the parties entered into prior to application for or issuance of anticipated but subsequently issued patents, can be enforced beyond the expiration dates of the patents. We hold that under the rule of per se invalidity established by *Brulotte* v. *Thys Co.*, 379 U.S. 29 (1964), the terms of a licensing agreement calling for royalty payments beyond the life of the patent are unenforceable where the parties enter the agreement with clear expectations that a valid patent will issue. We therefore reverse the order of the district court granting partial summary judgment for the plaintiffs and remand for proceedings consistent with this opinion.

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* Honorable Anna Diggs Taylor, United States District Court for the Eastern District of Michigan, sitting by designation.

FACTS

Over twenty years ago, the plaintiffs-appellees, Robert Boggild and William Dale, invented a toy extruder to be used with the modeling substance called Play-Doh. In January 1963, the plaintiffs granted Kutol Products, Inc. an exclusive license to make, use and sell the extruder in conjunction with its line of Play-Doh products. Kutol subsequently assigned its rights and obligations under the 1963 license agreement to the defendant-appellant, Kenner Products.[1] At the time the plaintiffs executed the agreement, no patents on the extruder had been issued or applied for. However, under Article II of the agreement, upon execution of the license the plaintiffs were required to promptly apply for mechanical and design patents on the extruder.[2] The plaintiffs' patent applications were subsequently issued with expiration dates of March 2, 1979 for the design patent and August 9, 1983 for the mechanical patent.

Under the agreement, Kenner, the licensee, was required to pay royalty payments for a minimum of twenty-five years from the date of the license, or January 18, 1988, regardless of whether the anticipated patents issued or not.[3] Thus, the

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[1] As found by the district court, the agreement was subsequently modified by a 1966 agreement between plaintiffs and Rainbow Crafts, Inc., also a predecessor in interest to Kenner, and by a 1971 agreement between plaintiffs and defendant Kenner Products Division. The 1963 agreement, however, is the only agreement pertinent to this appeal.

[2] Article II of the 1963 agreement, entitled "Patent Applications," provides:

> "B & D will promptly file and diligently prosecute at their expense both mechanical and design patent applications directed to said Extrusion Device in the United States and Canada.
>
> * * *
>
> "It is agreed that if B & D fails to file the patent applications in the United States and foreign countries specified above Kutol shall have the right to file the said applications and to deduct the costs of such filing from royalty payments owed to B & D."

[3] Article VI(g) of the agreement provides for royalty payments regardless of compliance with Article II:

agreement required the royalty payments to continue four and a half years beyond the latest patent expiration date.

In March 1983, the plaintiffs filed in state court a breach of contract action challenging the method used by Kenner to calculate royalties due on the selling price of the extruder devices. Kenner petitioned for removal to the federal district court and filed an answer to the plaintiffs' complaint. In its answer, Kenner generally denied that it improperly calculated royalties, and asserted two counterclaims. The first counterclaim alleged that the plaintiffs owed Kenner an amount of royalty overpayments. The second counterclaim alleged that due to the expiration of the patents, Kenner was no longer obligated to pay royalties, and, despite the terms of the agreement, was entitled to make, use and sell the toy extruders without further payments.

Upon consideration of the plaintiffs' motion for partial summary judgment on Kenner's second counterclaim, the district court determined that since the patents had issued after the parties entered into the licensing agreement, the agreement did not run afoul of the holding in *Brulotte* v. *Thys Co.*, 379 U.S. 29 (1964), prohibiting a patent licensor from using the leverage of its patent to extend royalty payments beyond the patent's seventeen year term. *Boggild* v. *Kenner Products*, 576 F.Supp. 533, 536-37 (S.D. Ohio 1983). Kenner appeals the district court's grant of partial summary judgment for the plaintiffs on Kenner's second counterclaim.

> It is agreed by the parties hereto that the royalty payments provided for herein shall be paid by Kutol regardless of whether or not the filing of the patent applications contemplated in Article II hereof results in the issuance of a patent or patents.

And, Article XIII(d), entitled "Termination", provides for royalty payments for a minimum of twenty-five years:

> (d) Unless previously terminated in accordance with the foregoing provisions of this Article XIII, this agreement and the rights granted hereunder shall run to the full end of the term or terms of any Letters Patent that may issue on or as a result of the application or applications referred to in Article II hereof or for a period of 25 years, whichever is longer, and shall thereupon terminate.

DISCUSSION

The underlying policy of patent law grants a seventeen year monopoly to an inventor in exchange for release of the invention to the public upon expiration of the patent. *Scott Paper Co.* v. *Marcalus Manufacturing Co.*, 326 U.S. 249, 255 (1945); *see Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 480-81 (1974); *Lear, Inc.* v. *Adkins*, 395 U.S. 653, 673-74 (1969); *Brulotte* v. *Thys Co.*, 379 U.S. 29, 30-31 (1964); *Prestole Corp.* v. *Tinnerman Products, Inc.*, 271 F.2d 146, 155 (6th Cir. 1959), *cert. denied*, 361 U.S. 964 (1960). Thus, for a limited time, the inventor exclusively reaps any material rewards from the invention on condition that she disclose it to the public upon expiration of the patent. *Scott Paper Co.* v. *Marcalus Manufacturing Co.*, 326 U.S. at 255. The extensive social and economic consequences of the patent "give the public a paramount interest in seeing that patent monopolies are kept within their legitimate scope." *Precision Instrument Mfg. Co.* v. *Automotive Maintenance Machinery Co.*, 324 U.S. 806, 816 (1945). Hence, efforts to extend or reserve the patent monopoly beyond the seventeen years contravene the policy and purpose of the patent laws. *Scott Paper Co.*, 326 U.S. at 255-56; *Prestole Corp.* v. *Tinnerman Products, Inc.*, 271 F.2d at 155.

Accordingly, in *Brulotte* v. *Thys Co.*, 379 U.S. 29 (1964), the Supreme Court found that an owner of patents on hop-picking techniques who executed licensing agreements requiring royalty payments beyond the life of the patent had improperly used the leverage of his patents to extend the monopoly. The patent owner issued a license for the use of each hop-picking machine sold to farmers for a flat sum. Under the license, hop farmers paid the greater of either a minimum royalty of $500 per hop-picking season or $3.33-⅓% per two hundred pounds of hops harvested by the machine. The license also prohibited assignment and removal of the machines from the county where sold. All of the patents incorporated into the machines expired before the licenses. Nonetheless, the royalties and restrictions required

under the licenses remained in identical effect both before and after the last patent expired.

The hop farmers eventually refused to pay royalties accruing both before and after the expiration of the patents. The patent owner sued to enforce the licenses under state contract law and the farmers defended with misuse of the patents through projection of royalties beyond the expiration date of the patents. The trial court enforced the licenses, however the Supreme Court of Washington affirmed.

The United States Supreme Court reversed. The Court determined that the license provisions described above were intrinsically designed to protect the privileges of the patent monopoly and that their identical application to the post-expiration period constituted a "bald attempt to exact the same terms and conditions for the period after the patents have expired as they do for the monopoly period." *Brulotte* v. *Thys Co.*, 379 U.S. at 32. The Court found that, by their terms, the royalties were for use during the post-expiration period and did not constitute deferred payment for use during the pre-expiration period or a sale of unpatented machines through long term payments based on a deferred purchase price. *Id.* at 31-32. Since the license provisions failed to distinguish between the pre-expiration and post-expiration periods, the Court was unable to determine whether the post-expiration royalties were subject to the leverage of the patent. *Id.* The Supreme Court concluded that under these circumstances the patent owner had abused the leverage of the monopoly to project royalties into the post-expiration period; the agreement, therefore, was unlawful *per se*. *Id.*

In the case at bar, the district court reasoned that the *Brulotte* rule of *per se* invalidity was inapplicable because, unlike the hop-picking patents in *Brulotte*, the toy extruder patents had not been issued at the time the parties entered into the licensing agreement. *Boggild* v. *Kenner Products*, 576 F.Supp. at 536-37. Thus, the district court distinguished the present case as one involving patents which issued after the agreement and which conferred "hybrid" rights entailing

trade secrets as well as "potential patent rights in part." *Id.* The district court then rejected the Eleventh Circuit's holding in *Pitney Bowes, Inc.* v. *Mestre*, 701 F.2d 1365 (11th Cir.), *cert. denied*, 104 S.Ct. 239 (1983), which concluded that the *Brulotte* rule of *per se* invalidity could be applied to hybrid agreements executed while applications for patents were pending:

> In our view the Eleventh Circuit over extended the *Brulotte* rule. It is clear from that early case that the Supreme Court found that the agreement, on its face, revealed an improper leveraging of the patent monopoly. In *Brulotte*, the patents had issued; thus the patentee had something that he could leverage. Here, no application had been made. We recognize that, regardless of whether an application had been made, one might improperly leverage the possibility that a patent might issue if the parties believe there is a substantial likelihood that a patent might issue. Under those circumstances, however, application of a per se rule is inappropriate. We hold, therefore, that the per se rule of *Brulotte* does not extend to the case where no patent application has been made at the time the agreement is negotiated even if an application is contemplated.

576 F.Supp. at 536-37. We reverse this judgment and hold that the *Brulotte* rule of *per se* invalidity precludes enforcement of license provisions which were developed in anticipation of patent protection and which require royalty payments for use, sale or manufacture of a patented item beyond the life of the patent.

The Eleventh Circuit's decision in *Pitney Bowes, Inc.* v. *Mestre*, is significant for several reasons. In *Mestre*, a prospective patent owner executed four licenses for the sole and exclusive rights to make and sell four different paper handling machines. Three of the agreements licensed both patent rights and trade secrets, one licensed only trade secrets,[4] but all four

[4] The district court found that one agreement entitled the "Rotary Col-

agreements entitled Mestre to collect royalties on each machine. As in the case at bar, patents for the machines issued after execution of the agreements. However, unlike plaintiffs Boggild and Dale, Mestre had filed patent applications before the agreements were struck. Also, as in *Brulotte* and the case at bar, the royalty and use provisions did not distinguish between rates of payment for the pre-expiration and post-expiration periods or between royalties attributable to the patent rights and those for any other rights. Finally, like *Brulotte* and this case, the termination provisions in the *Mestre* agreements extended "hybrid" royalty payments beyond the life of the patent.

The United States District Court for the Southern District of Florida rejected Mestre's contention that the post-expiration royalties were attributable to the license for trade secrets and found that the hybrid agreement and Mestre's right to collect royalties thereunder ended upon expiration of the patent. *Pitney Bowes, Inc.* v. *Mestre*, 517 F.Supp. 52, 63 (S.D. Florida 1981). The Eleventh Circuit affirmed, ruling moreover that *Brulotte* was applicable to hybrid agreements and that issuance of the pending patent precluded enforcement of conflicting trade secret provisions. The circuit court found that under *Brulotte*, the agreement was invalid *per se* because the agreement's terms for royalty payments and exclusive use applied equally before and after expiration of the patent. 701 F.2d at 1373. Thus, the Eleventh Circuit found improper leveraging of the patent monopoly by applying *Brulotte's* rationale of *per se* invalidity to an agreement where the patents had not issued at the time of licensing but were

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lator Agreement" licensed trade secret rights only. 517 F.Supp. at 62. However, the Eleventh Circuit noted that during oral argument on appeal, Mestre conceded that like the other three, the Rotary Collator Agreement was a hybrid license for both patent rights and trade secrets. 701 F.2d at 1373 n.13. The Court of Appeals invited the district court to consider Mestre's concession and to apply *Brulotte* to the Rotary Collator Agreement as well. *Id.* Both the district court and Court of Appeals equated trade secrets with "know-how.". 517 F.Supp. 54 n.la; 701 F.2d at 1367 n.4.

pending and where trade secret rights were expressly included with patent rights.

We agree with the Eleventh Circuit that once the pending patent issues, enforcement of royalty provisions for other rights which conflict with and are indistinguishable from royalties for patent rights, is precluded. As noted in *Mestre*, the Supreme Court has upheld enforcement of potentially conflicting state trade secret provisions in hybrid agreements *only where no patents ever issued. See Aronson* v. *Quick Point Pencil Co.*, 440 U.S. 257 (1979);[5] *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470 (1974). Upon issuance of the patent, however, federal supremacy requires directly conflicting provisions to be resolved under federal patent law. *Pitney Bowes, Inc.* v. *Mestre*, 701 F.2d at 1372.

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[5] In our view, *Aronson*, lends further support to the contention that the *Brulotte* rule of *per se* invalidity is applicable to hybrid agreements in which royalties for patent rights are indistinguishable from those for other rights. In *Aronson* the Supreme Court reversed an Eighth Circuit decision applying *Brulotte* to terms of an agreement which provided for a 5% royalty for exclusive rights to a keyholder design but reduced royalty payments if the inventor failed to obtain a patent within five years after the agreement. The patent applications failed and the reduced royalties became effective for an indefinite term. The Eighth Circuit concluded that had the pending patent issued, royalty payments could not have continued beyond the 17 year monopoly period. The Eighth Circuit reversed the district court judgment enforcing the terms of the agreement. *Quick Point Pencil Co.* v. *Aronson*, 567 F.2d 757 (8th Cir. 1977). The Supreme Court reversed and held that absent issuance of a patent, federal patent law does not preempt state contract law. The Court concluded the terms of the agreement contravened no purpose under the federal patent system and that the reduced royalty was not negotiated with the leverage of a patent. 440 U.S. at 265. In so holding, however, the Court specifically noted that had the patent issued, enforcement of the higher 5% royalty rate for exclusive rights beyond the life of the patent would have been precluded:

> "Mrs. Aronson attempted to obtain a patent for over five years. It is quite true that had she succeeded, she would have received a 5% royalty only on keyholders sold during the 17-year life of the patent."

440 U.S. at 263-64. Thus, the Court would presumably have applied *Brulotte* to a "hybrid" agreement embodying rights conferred under both state law and the federal patent law.

We also agree with the Eleventh Circuit that misuse of the leverage afforded by a pending patent is subject to the *Brulotte* rule of *per se* invalidity. In *Aronson* v. *Quick Point Pencil Co.*, 440 U.S. 267 (1979) the Supreme Court acknowledged the leverage afforded to a patent owner by a pending patent application. Although the Court refrained from defining what constitutes abuse of such leverage, it described the nature of the leverage and the inquiry upon examination for abuse:

> No doubt a pending patent application gives the applicant some additional bargaining power for purposes of negotiating a royalty agreement. The pending application allows the inventor to hold out the hope of an exclusive right to exploit the idea, as well as the threat that the other party will be prevented from using the idea for 17 years. However, the amount of leverage arising from a patent application depends on how likely the parties consider it to be that a valid patent will issue.

440 U.S. at 265.

In *Mestre*, the agreement expressly referred to the pending patent applications, *see* 701 F.2d at 1370 n.9, and several of its provisions would become enforceable only if the patents issued. On these facts, the Eleventh Circuit concluded that the parties had anticipated issuance of the patents and that Mestre had obtained sufficient leverage from the pending patents to warrant application of the analysis in *Brulotte*.

In our view, the same violations of patent law arising from abuse of the leverage attached to a pending or issued patent can arise from abuse of the leverage afforded by an expressly anticipated application for a patent. The agreement at bar aptly demonstrates this contention. As noted in the facts section of this opinion, Article II of the licensing agreement required the plaintiffs "to promptly file and diligently prosecute mechanical and design patent applications" for the toy extruder. In fact the parties decreed in Article VI that no royalties would be paid until the plaintiffs applied for the mechanical patent.

Throughout the licensing agreement, similar provisions reiterate the parties' anticipation and expectation of successful patent applications. Article IV of the agreement grants the exclusive right to manufacture, use and sell the licensed extruder. Article X provides that the defendant Kenner will admit the validity of any "patent under which rights herein are granted." Article XII gives Kenner the sole right to proceed against infringers of "any patents granted on the applications or inventions herein licensed." And subparagraph (c) of Article XIII suggests the entire license was premised upon this issuance of patents: it gives Kenner the right to terminate the license in the event of unlicensed competition which the parties "are unable or unwilling to prevent or restrain." Paragraph XIV, entitled "Patent Infringement Search", required the plaintiffs to commission a patent infringement search by a reputable patent law firm within thirty days after execution of the agreement in order to determine the likelihood of receiving a patent. Moreover, as noted above in footnote 3 of this opinion, the termination provisions of Article XIII(d) not only contemplate the anticipated patents but expressly require all terms of the agreement to run a minimum of twenty-five years, four and a half years beyond the life of the subsequently issued mechanical patent.

Thus, the tenor of the licensing agreement compels us to find that the possibility of forthcoming patents on the toy extruder substantially contributed to the formation of the licensing agreement and that the parties assumed a high likelihood that valid patents would issue. The terms of the licensing agreement compel the conclusion that, at the time the parties executed the license, the plaintiffs exerted considerable leverage from the anticipated patents. In our view, the absence of a filed patent application is, under these circumstances, irrelevant to the analysis under *Brulotte*.

Having established the leverage from anticipated patents, our inquiry next focuses on whether such leverage was misused to project the monopoly beyond the life of the patent. In *Brulotte* the Supreme Court found a *per se* projection of the monopoly where the provisions protecting the exclusive rights

conferred by the patent applied without change to the post expiration period and where royalties for use during the patent were indistinguishable from royalties due after expiration. *Brulotte* v. *Thys Co.*, 379 U.S. at 32. In the case at bar, the agreement calls for royalties on the sales of the patented extruder for a minimum of twenty-five years.[6] As in *Brulotte*, the agreement contains neither provisions for reduction of royalties in the event valid patents never issued nor terms for reduction of post-expiration royalties. The provisions for use of the extruder and payment of royalties are applicable to both the pre-expiration and post-expiration periods. Therefore, under *Brulotte*, the agreement is unlawful *per se*.

Accordingly, the district court's grant of partial summary judgment to the plaintiffs is hereby reversed.

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[6] Although Article VI of the agreement requires royalty payments whether the patents issued or not, the only royalties required are those on sales of the patent device. In light of the parties' clear contemplation of successful patent applications, the disclaimed relevance of the patent in Article VI must be discounted.

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

C-1-83-638

ROBERT BOGGILD,
and
WILLIAM L. DALE,
Plaintiffs,

vs.

KENNER PRODUCTS, Division of
GENERAL MILLS FUND GROUP, INC.,
Defendant.

OPINION AND ORDER GRANTING PLAINTIFF'S MOTION FOR PARTIAL JUDGMENT ON THE PLEADINGS AND DENYING DEFENDANT'S MOTION FOR PARTIAL SUMMARY JUDGMENT

[Filed December 15, 1983]

SPIEGEL, J.:

This matter came on for hearing on the plaintiffs' motion for partial judgment on the pleadings with respect to defendant's eighth affirmative offense and second counterclaim (doc. 8) and defendant's cross-motion for partial summary judgment on its second counterclaim, or in the alternative to suspend both motions so that discovery with respect to these motions can be conducted (doc. 9). Defendant filed a memorandum in opposition to plaintiffs' motion and in support of its own motion (doc. 10) and a reply memorandum (doc. 15). Plaintiffs filed a reply memorandum in support of their motion and opposing defendant's motion (doc. 14).

Defendant's alternative motion to suspend both motions is denied as we find that additional discovery is not necessary to

decide the issues presented to us by the cross-motions. We find that there are no genuine issues of material fact with respect to defendant's second counterclaim and eighth affirmative defense and further that plaintiff is entitled to judgment as a matter of law on that counterclaim and defense. Accordingly, defendant's motion is denied. Plaintiffs' motion is granted.

Underlying this action is a toy extruder device invented by plaintiffs. That device is the subject of an agreement and its amendments under which plaintiffs granted exclusive rights to the invention to Kutol Products, Inc. (*see* complaint, exh. A). Kutol, Kenner's predecessor in interest, subsequently assigned its rights and obligations under the agreement to defendant Kenner.

The parties entered into the licensing agreement January 18, 1963.[1] Plaintiff subsequently applied for mechanical and design patents on their invention as required by Article II of the agreement. Both patents issued. The design patent expired March 2, 1979; the mechanical patent, August 9, 1983.

Plaintiffs brought this action challenging the way in which defendant has calculated royalties and alleging unauthorized use without payment of royalties. They seek an accounting and damages.

Defendant filed an answer in which it asserted two counterclaims, the second of which is the subject of these motions. That counterclaim seeks a declaration that as of August 9, 1983, when the second patent expired, defendant owed no further obligation to pay royalties to plaintiffs under the licensing agreement and may manufacture, use and sell the device disclosed or claimed in the two patents disclosing the extruder device without obligation to plaintiffs. This counterclaim is the obverse of defendant's eighth affirmative

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[1] This agreement was subsequently modified by a 1966 agreement between plaintiffs and Rainbow Crafts, Inc., also a predecessor in interest of the present defendant, and by a 1971 agreement between plaintiffs and defendant, Kenner Products Division. The 1963 agreement, however, is the only agreement pertinent to these cross-motions.

defense, which asserts that the expiration of the patents covering the device bars plaintiffs from enforcing the licensing agreement.

Article IV of the agreement gives defendant the exclusive right to manufacture, use and sell the licensed extruder device. Article II requires that plaintiffs file patent applications covering the device. Article VI(g), however, states:

> It is agreed by the parties hereto that the royalty payments provided for herein shall be paid by Kutol regardless of whether or not the filing of the patent applications contemplated in Article II hereof results in the issuance of a patent or patents.

Article XIII(d) of the agreement provides:

> Unless previously terminated in accordance with the foregoing provisions of this Article XIII, this Agreement and the rights granted hereunder shall run to the full end of the term or terms of any Letters Patent that may issue on or as a result of the application or applications referred to Article II hereof or for a period of 25 years, whichever is longer, and shall thereupon terminate.

As noted, the last of the applicable patents expired August 9, 1983. The twenty-five year period from the date of the license agreement will not expire until January 18, 1988.

The unambiguous language of the agreement makes it clear that the parties intended that royalty payments would continue whether or not the patents issued. Further, the payments would continue for a minimum of twenty-five years.

It is also undisputed that the inventors had not yet applied for patents covering the extruder device at the time the agreement was entered into. The agreement thus involved the disclosure and licensing by Boggild and Dale to Kutol of certain confidential information in the form of finished drawings of the design and a working model of the extrusion device.

Defendant's eighth affirmative defense and second counterclaim are grounded upon the proposition that the licensing

agreement loses its validity and enforceability upon the expiration of the patents covering the licensed device. In effect, defendant argues that once the patents issued, plaintiffs lost the protection of state trade secret and/or contract law in exchange for the patent protection conferred by federal law. Defendant frames the issue raised by the cross-motions thusly:

> [W]hether a license agreement that expressly provides for the payment of royalties on the sales of defined subject matter for a term extending beyond the life of a patent which was contemplated by the contract to cover the defined subject matter and which in fact does cover it is enforceable for the full term expressed by the agreement regardless of the expiration date of the patent, or whether the agreement becomes unenforceable as a matter of law upon the expiration of the patents.

(doc. 10 at 1-2). Defendant relies on *Brulotte* v. *Thys Co.*, 379 U.S. 29, 32 (1964) in which the United States Supreme Court held that regardless of state contract law, a licensing agreement that extends a patent's monopoly beyond the life of the patent involved is a per se violation of federal patent law. Defendant concludes that the licensing agreement became violative of federal law and thus unenforceable as of August 9, 1983 when the latter patent expired.

It is fundamental that any attempt to continue "the patent monopoly, after the patent expires, whatever the legal device employed, runs counter to the policy and purpose of the patent laws." *Scott Paper Co.* v. *Marcalus Co.*, 326 U.S. 249, 256 (1945) quoted in *Brulotte*, 379 U.S. at 31. In *Brulotte* the Supreme Court held that royalty provisions of a licensing agreement covering the use of machines incorporating certain patents are not enforceable beyond the expiration of the last patent incorporated in the machine. The court observed that a patentee may use his patent to exact the highest royalties possible, using his monopoly as leverage. 379 U.S. at 33. However, it held unlawful per se a patentee's use of a royalty agreement extending beyond the date of the patent. 379 U.S. at 32.

As plaintiffs point out, the facts of *Brulotte* are distinguishable. The royalty agreements in *Brulotte* issued in connection with the sale of machines incorporating seven patents, all of which had isued prior to the execution of the agreements, and licensed the use of the patent ideas. Thus the rights licensed were exclusively patent rights. In the present case, however, the agreement preceded the patents and thus the rights licensed are more properly characterized as trade secret rights — at least in part — and potential patent rights in part.

Defendant's response is that *Brulotte's* per se rule extends to agreements where a patent is applied for and issues after the agreement is negotiated. Defendant refers to *Pitney Bowes, Inc.* v. *Mestre*, 701 F.2d 1365 (11th Cir. 1983), *cert. denied*, 52 U.S.L.W. 3291 (Oct. 11, 1983).

At issue in *Mestre* was a hybrid agreement licensing both patent rights and trade secret rights and providing for royalties in exchange for the sale and exclusive right to manufacture and sell a machine described in then pending patent applications. The agreement expired on the latest of three dates — the patentee's death, after seventeen years, or when the last patent on the machine expired. The last patent expired approximately eighteen months prior to the patentee's death. The Eleventh Circuit held that the agreement was unenforceable under *Brulotte* on the grounds that two provisions suggested that the patentee used the leverage of his patent to extend the monopoly beyond the seventeen year patent period. First, the exclusive rights licensed under the agreement applied equally before and after expiration of the patent and second, the agreement required the licensee to pay royalties at the same rate and on the same basis both before and after expiration of the patent. 701 F.2d at 1373.

In our view the Eleventh Circuit over extended the *Brulotte* rule. It is clear fr m that early case that the Supreme Court found that the agreement, on its face, revealed an improper leveraging of the patent monopoly. In *Brulotte*, the patents had issued; thus the patentee had something that he could leverage. Here, no application had been made. We recognize that, regardless of whether an application has been

made, one might improperly leverage the possibility that a patent might issue if the parties believe there is a substantial likelihood that a patent might issue. Under those circumstances, however, application of a per se rule is inappropriate. We hold, therefore, that the per se rule of *Brulotte* does not extend to the case where no patent application has been made at the time the agreement is negotiated even if an application is contemplated.

That, however, is not the end of our inquiry, for in this case patents did issue. We must, therefore, consider the proper relationship between federal patent law and state law in such a situation.

The test we must apply is whether state law which would otherwise render this agreement enforceable "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Hines* v. *Davidowitz*, 312 U.S. 52, 67 (1941), quoted in *Aronson* v. *Quick Point Pencil Co.*, 440 U.S. 257, 262 (1979). If state law does not present such an obstacle, then state law governs. Conversely, if state law otherwise rendering this agreement enforceable conflicts with federal law, then federal law governs.

As a preliminary matter, we note the clear distinction between the protection afforded by federal patent law and that available under state trade secret law. Under federal patent law, the inventor of a patentable "useful process, machine, manufacture, or composition of matter, or . . . useful improvement thereof," 35 U.S.C. § 101, is granted an exclusive monopoly to sell or use his invention for seventeen years, at the end of which the invention will be disclosed to the public. 35 U.S.C. § 154; *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 480-81 (1974). Trade secrets, on the other hand, may or may not be patentable. The holder of a trade secret is protected against the disclosure or unauthorized use of the trade secret by those to whom it has been confided on condition that the secret not be disclosed. The holder is also protected against use of the trade secret where knowledge of the trade secret has been acquired by some improper means. O.R.C. § 1333.51; Restatement of Torts § 757(a). However, although

the protection accorded a trade secret holder is for an indefinite period of time, the holder — unlike the patentee — runs the risk that his secret may be discovered through proper means such as independent invention or reverse engineering. In that event, the trade secret holder cannot prevent disclosure or use of his secret, unlike the patentee who can do so if his patent is not yet expired.

The Supreme Court has held that state trade secret law is not preempted by federal patent law. *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470 (1974). With respect to clearly patentable inventions, the Court found that extending trade secret protection to such inventions does not conflict with the patent policy of disclosure. *Id.* at 489-93.

Kewanee, however, was an action seeking relief from the misappropriation of trade secrets and was based upon employment agreements requiring the non-disclosure of confidential information or trade secrets obtained as employees. The case thus did not present the issue of how royalty payments should be treated where licensed ideas were accorded the protection of federal patent law after the parties entered into a licensing agreement.

The Supreme Court subsequently held that state contract law is not preempted by federal patent law in an action to enforce a contract to pay royalties to a patent applicant on sales of goods involving the putative invention where the patent was not granted. *Aronson* v. *Quick Point Pencil Co.*, 440 U.S. 257 (1979). While Mrs. Aronson's patent application was pending, Quick Point entered into a contract with her pursuant to which it would pay her five percent of the selling price in exchange for the exclusive right to make and sell the keyholder covered by her pending application. The contract further provided that if the patent did not issue within five years, Quick Point would pay a royalty of two and one-half percent of sales so long as Quick Point continued to sell the keyholder. No patent issued.

Quick Point subsequently brought an action to have the contract declared unenforceable on the ground that state contract law — which might otherwise make the contract en-

forceable — was preempted by federal law. The Supreme Court noted that at the time the contract was executed, the parties knew about the pending patent application and recognized the possibility that a patent might not issue. The Court observed that despite the uncertainty of patent protection, Quick Point obviously placed a significant value on being the first to exploit the basic novelty of the keyholder. *Id.* at 261-62.

On these facts, the Supreme Court found no conflict with any of the three goals of patent law: incentive to invention, disclosure, and the policy against withdrawing ideas from the public domain. The Court found that state contract law provided an additional incentive to invention and that encouraging inventors to arrange for the manufacture of their inventions furthered the federal policy of disclosing inventions. Finally, it found that enforcing a contractual obligation to pay royalties does not conflict with federal policy against withdrawing ideas from the public domain because enforcement would not withdraw the idea from the public domain. The Court reasoned that Mrs. Aronson's idea entered the public domain as a result of the agreement licensing the manufacture and sale of her invention. *Id.* at 262-63. The Court maintained that its reasoning was consistent with that of *Brulotte* because on this record it was clear that although the pending application may have served Mrs. Aronson as leverage, that leverage was not abused as the reduced royalty provision revealed that both parties recognized a substantial likelihood that the patent would not issue. *Id.* at 264-65.

Defendant insists that *Aronson* is not applicable as no patent issued in that case and thus there could be no conflict between federal and state law. Further defendant maintains that the language of *Aronson* makes it clear that *Aronson* does not apply where a patent does issue. Defendant points out that its interpretation of the *Aronson* decision is consistent with the Eleventh Circuit's analysis of *Aronson* in *Pitney Bowes, Inc. v. Mestre*, 701 F.2d 1365 (11th Cir. 1983), *cert. denied*, 52 U.S.L.W. 3291 (Oct. 11, 1983). Finally, it insists that a proper reading of Supreme Court cases leads inevitably

to the conclusion that the Eleventh Circuit's reasoning in *Mestre* must be applied to the instant case.

As discussed earlier, *Mestre*, like *Aronson* and the instant case, involved a hybrid agreement. The Eleventh Circuit stated that in its view, and despite *Kewanee* and *Aronson*, the Supreme Court did not "necessarily" intend full trade secret protection where a patent issues subsequent to an agreement to pay royalties. It then stated:

> *When a patent issues, the potential exists for direct conflict between federal patent law and state trade secret law.* When such a conflict occurs, the question is no longer one of federal preemption; it is instead one of federal supremacy.

Id. at 1372 (footnote omitted) (emphasis added). In other words, under the *Mestre* analysis, where a patent has issued, the Court must determine not whether federal law preempts but rather whether there is a conflict between federal and state law.

Because patents issued in this case, the question is not one of preemption, but rather of supremacy, as the Eleventh Circuit stated. However, in resolving a supremacy issue as in resolving a preemption issue, the fundamental question is whether there is a conflict. The Supreme Court's preemption discussions are thus critical to our own analysis.

The one principle that clearly emerges is that we must examine the agreement in light of the purposes of the federal patent law. Those purposes are well established: to foster and reward invention; to foster disclosure of inventions in order to stimulate further innovation and to permit the public to practice the invention following expiration of the patents; and to assure that ideas in the public domain remain there for the free use of the public. *Aronson*, 440 U.S. at 262, citing *Kewanee*, 416 U.S. at 480-81. We conclude that enforcing this agreement will not conflict with any one of these purposes.

First, the Supreme Court has already stated that permitting inventors to make enforceable licensing agreements in ex-

change for royalties provides an additional incentive to invention and thus is consistent with federal policy. *Aronson*, 440 U.S. at 262. We find that this incentive exists whether or not a patent issues. Secondly, the Supreme Court has stated that encouraging inventors to arrange for the manufacture of their inventions furthers the policy of disclosure because each manufactured item discloses the invention. *Aronson*, 440 U.S. at 262-63. The situation is similar here; the effect of the agreement was to disclose the extruder device to the public. The agreement does not give the plaintiffs protection beyond that available to them under the patent law. As of the expiration of the last patent, any member of the public may manufacture, use, or sell the device. All the agreement requires is that the defendant continue to pay for the privilege of having been first in the market place. And third, enforcing a contract for royalties does not conflict with the policy against withdrawing ideas from the public domain. *Aronson*, 440 U.S. at 263. That policy is executed by issuing patents only to inventions that meet the exacting standards enacted by Congress. The agreement required the plaintiffs to seek the added protection of the patent law on behalf of the defendant. The effect of the patent was to withdraw the idea from the public domain for seventeen years. Now that the patents have expired the idea is in the public domain. All this agreement requires is that the defendant continue to pay royalties — as it agreed to do — for a period of time in exchange for the advantage of having been the first manufacturer of the device.

Even though there is no conflict with federal patent law, we are nonetheless left with the question posed by *Scott Paper* and *Brulotte:* whether the plaintiffs used the leverage of a patent to extract rights that would not otherwise be available to them and that went beyond the rights available to them under the federal patent law. *Scott Paper* prohibits the use of any legal device to extend the patent monopoly beyond the expiration of the patent. 326 U.S. at 256. *Brulotte* forbids the use of a patent monopoly as leverage to project the patent monopoly beyond the term of the patent. 379 U.S. at 32.

The answer to this question is located in the fact that the

agreement at issue is one for the payment of royalties. Plaintiffs are not invoking the indeterminate protection of Ohio trade secret law. They are not seeking to prevent the public from manufacturing, selling or using this invention. Rather they seek to enforce the bargain they negotiated with defendant, *i.e.*, the payment of royalties for a specified period in exchange for defendant's having the advantage of being first in the market place. We also note that it was defendant — rather than plaintiffs — who primarily benefitted from the protection of the federal patent law. We conclude, therefore, that plaintiffs did not use this agreement to extend their patent monopoly beyond the terms of the patents. Moreover, we conclude that even if plaintiffs did use the possibility that their invention might be patentable as leverage, that leverage was not used to project the patent monopoly but rather to extract higher royalties. Accordingly, we find that this agreement does not fall within the prohibitions of *Scott Paper* and *Brulotte*.

We recognize that in *Aronson*, the Supreme Court concluded that Mrs. Aronson had not improperly leveraged her pending application because the agreement provided for lower royalties if the patent did not issue. 440 U.S. at 264-65. The parties in our case did not include such a provision which could make such a conclusion inevitable. That language, however, is dicta. More important, nothing in *Aronson* suggest that an inventor may not use the possibility that his idea is patentable as leverage. What is prohibited is using that leverage to extend a patent monopoly. We read *Scott Paper*, *Brulotte*, and *Aronson*, as permitting an inventor to leverage the possibility that his invention is patentable for the purpose of extracting more advantageous royalty terms for a specified and reasonable period of time even if subsequent to the agreement a patent does issue but the patent expires before the negotiated period over which royalties are payable.

In the instant case, it is unnecessary to determine whether plaintiffs used the possibility that their invention was patentable as leverage. It is clear from the undisputed facts that even if that possibility was leveraged it was for the purpose of

extracting higher royalties, not of unlawfully extending the patent monopoly.

To summarize, what the defendant negotiated for in this case was for the right to be first in the marketplace with a novel idea. The parties drafted an agreement which made it clear that the defendant was willing to pay for that right whether or not the patent issued. In the event the patent issued the defendant would have additional protections. We simply see no way in which this conflicts with any of the three stated and clearly recognized purposes of the federal patent law. We find that state law does not stand as "an obstacle to the accomplishment and execution of the sole purposes and objectives" of federal patent law. *Hines*, 312 U.S. at 67.

We find further that the language of the agreement reveals that this agreement is not an attempt to extend a patent monopoly beyond the term of the patent. Moreover, we find that because plaintiffs did not seek to extend the patent monopoly beyond its term, whether they leveraged the possibility that their invention was patentable is not material. Accordingly, we conclude that this agreement for the payment of royalties is enforceable under state law.

As there are no disputed issues of material fact, we hold that plaintiffs are entitled to judgment as a matter of law on defendant's second counterclaim and defendant's eighth affirmative defense. Accordingly, judgment is hereby entered against defendant and for plaintiffs on defendant's second counterclaim.

SO ORDERED.

/s/ S. ARTHUR SPIEGEL
United States District Judge

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 84-3467

ROBERT BOGGILD, WILLIAM L. DALE,
Plaintiffs-Appellees,

v.

KENNER PRODUCTS, Division of CPG Products Corp.,
Defendant-Appellant.

Before: KEITH and MARTIN, Circuit Judges; and
TAYLOR, District Judge.

JUDGMENT

[Filed November 13, 1985]

ON APPEAL from the United States District Court for the Southern District of Ohio.

THIS CAUSE came on to be heard on the record from the said District Court and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this court that the judgment of the said District Court in this case be and the same is hereby reversed and the case is remanded for proceedings consistent with this opinion.

It is further ordered that Defendant-Appellant recover from Plaintiffs-Appellees the costs on appeal, as itemized below, and that execution therefor issue out of said District Court, if necessary.

ENTERED BY ORDER OF THE
COURT

John P. Hehman, Clerk

/s/ JOHN P. HEHMAN,
Clerk

Issued as Mandate: January 9, 1986
COSTS: Awarded to appellant

Filing fee	$ 70.00
Printing	$506.40
Total	$576.40

A True Copy.
Attest:
/s/
Deputy Clerk

No. 84-3467

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

ROBERT BOGGILD, WILLIAM L. DALE,
Plaintiffs-Appellees,

v.

KENNER PRODUCTS, A DIVISION OF
CPG PRODUCTS CORP.,
Defendant-Appellant.

ORDER

[Filed January 2, 1986]

Before: KEITH and MARTIN, Circuit Judges; and DIGGS TAYLOR*, United States District Judge

The Court having received a petition for rehearing en banc, and the petition having been circulated not only to the original panel members but also to all other active judges of this Court, and no judge of this Court having requested a vote on the suggestion for rehearing en banc, the petition for rehearing has been referred to the original hearing panel.

The panel has further reviewed the petition for rehearing and concludes that the issues raised in the petition were fully considered upon the original submission and decision of the case. Accordingly, the petition is denied.

ENTERED BY ORDER OF THE
COURT

/s/ JOHN P. HEHMAN, Clerk

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* Hon. Anna Diggs Taylor sitting by designation from the Eastern District of Michigan.

1963 LICENSE AGREEMENT

AGREEMENT

This Agreement dated as the 18th day of January, 1963 and effective as of that date, by and between Robert Boggild and William L. Dale, individuals, both residing in the City of Cincinnati, Ohio (hereinafter referred to as B & D) and Kutol Products, Inc., a corporation of Ohio having its principal place of business at Cincinnati, Ohio (hereinafter referred to as Kutol), witnesseth:

WHEREAS, B & D *developed certain information* relating to an Extrusion Device and have disclosed such information to Kutol by means of finished drawings copies of which are attached as Exhibit A and a working model; and

WHEREAS, Kutol is desirous of utilizing *said information* and to manufacture and sell said Extrusion Devices, and B & D is willing to grant such rights for the purposes and on the conditions hereinafter set forth:

NOW, THEREFORE, in consideration of the premises and the mutual covenants of this agreement, the parties hereto agree as follows:

I. SCOPE OF AGREEMENT

The field and scope of this agreement and the rights and obligations set forth herein shall be limited to a toy Extrusion Device of the general type and substantially in accordance with the prior disclosure to Kutol by B & D and includes an extruder for manually forcing modeling compound through dies of varying shapes.

II. PATENT APPLICATIONS

B & D will promptly file and diligently prosecute at their expense both mechanical and design patent applications directed to said Extrusion Device in the United States and Canada.

B & D shall file patent applications directed to said Extrusion Devices in the United Kingdom, France, Germany and Italy.

To prevent inadvertent bars to valid patent protection prior to the filing of the United States mechanical patent application Kutol agrees to give B & D 15 days advance notice that said Extrusion Devices will be put on sale or in public use or will be described in a printed publication.

It is agreed that if B & D fails to file the patent applications in the United States and foreign countries specified above Kutol shall have the right to file the said applications and to deduct the costs of such filing from royalty payments owed to B & D.

III. TRADEMARKS

Any and all trademarks and tradenames used in connection with the sale of the devices which are the subject matter of this agreement, together with the good will of the business founded thereon shall be the property of Kutol.

IV. RIGHTS GRANTED

(a) B & D hereby grants to Kutol and Kutol hereby accepts, subject to the covenants and conditions hereinafter expressed, the exclusive right, license and privilege of manufacturing and of using and selling throughout the world and including the exclusive right to sue for infringement, the aforesaid Extrusion Devices constructed in accordance with inventions and improvements hereinafter identified during the term of this agreement which shall remain *exclusive with Kutol subject to the conditions hereinafter expressed.*

(b) B & D hereby grants to Kutol the exclusive worldwide rights to any improvements upon the subject matter of this agreement that may be made by B & D during the life of this agreement, which shall come under the terms of this agreement and shall be available to Kutol without any additional royalty payments over and above that hereinafter specified.

(c) B & D hereby grants to Kutol any improvements

made by others on Extrusion Devices which are the subject matter of this agreement, which B & D may acquire, or come under its control, during the life of this agreement, which improvements shall be the property of, and properly assigned to Kutol to the full extent of B & D's interest therein.

(d) B & D hereby grants to Kutol and Kutol hereby accepts, subject to the covenants and conditions herein expressed, the right to grant to other manufacturers throughout the world, sublicenses to manufacture, use and sell the Extrusion Devices.

V. TECHNICAL ASSISTANCE

B & D will provide engineering drawings suitable for use in purchasing of required parts and design of tooling and will further provide working models of said Extrusion Device having a pleasing appearance of a quality sufficient to demonstrate the product to potential customers. B & D will participate in negotiations to obtain suppliers for parts and will work with parts manufacturers and/or assemblers until the product is established in satisfactory repetitive manufacture and will redesign the devices as required to eliminate any design or mechanical faults that appear after manufacture is started. B & D will further establish standards for manufacture of the device and agree to communicate to Kutol any technical knowhow, data or other information pertinent to the subject devices which are now in B & D's possession or which may hereinafter within the term of this agreement be acquired by B & D.

B & D will provide similar technical assistance to sublicensees of Kutol, reasonable charges for services and expenses to be borne by licensees.

VI. REPORTS AND ROYALTIES

(a) During the term of this agreement, Kutol shall make written reports to B & D within fifteen (15) days after the last day of the preceding month, stating in such reports the number of Extrusion Devices sold or otherwise disposed of during

the month for which a report is rendered. The first such report shall include all Extrusion Devices sold or otherwise disposed of between the date of this agreement and the terminal date of such report.

(b) Kutol also agrees to continue making monthly reports to B & D after the date of any termination of this agreement, stating in such report, the number of Extrusion Devices sold or otherwise disposed of hereunder and not previously reported to B & D until the complete inventory of devices has been sold or otherwise disposed of.

(c) The expression "sold or otherwise disposed of" shall include in its meaning (1) those devices not sold but delivered by Kutol to others regardless of the basis for compensation if any; and (2) devices put into use by Kutol for any purpose other than routine testing of such devices.

(d) Under this agreement, Extrusion Devices shall be considered to be sold when billed out. Royalties paid on any devices which are not accepted by Kutol customers for any reason, however, shall be credited to Kutol.

(e) In order to insure to B & D the full royalty payments contemplated hereunder, Kutol covenants that, in the event that any Extrusion Devices licensed hereunder shall be sold for resale either (1) to a corporation, firm or association which, or individual who, shall own a controlling interest in Kutol by stock ownership or otherwise, or (2) to a corporation, firm, or association in which Kutol or its stockholders shall own a controlling interest by stock ownership or otherwise, the royalties to be paid hereunder in respect to such devices shall be based upon the selling price at which such purchaser resells such devices, rather than upon the net selling price of Kutol.

(f) Concurrently with the making of any report under this agreement, Kutol shall pay to B & D royalties in accordance with the following schedule:

(1) Three (3%) per cent of the "on the dock" selling price for the first 100,000 Extrusion Devices; four (4%) per cent of the "on the dock" selling price for

all Extrusion Devices between 100,000 and 500,000; and five (5%) per cent of the "on the dock" selling price for all Extrusion Devices sold in excess of 500,000 by Kutol and its United States licensees and assigns.

(2) Accessories designed by B & D and licensed hereunder to Kutol for use with the extruder and sold separately shall be subject to the same royalty schedule as Item (1) above.

"On the dock" selling price is defined as Kutol's or its licensee's invoice price of the final packaged product as sold to a buyer not controlled by Kutol or its licensees as defined in Article VI (e).

(g) It is agreed by the parties hereto that the royalty payments provided for herein shall be paid by Kutol regardless of whether or not the filing of the patent applications contemplated in Article II hereof results in the issuance of a patent or patents.

(h) In event royalties accrued and paid hereunder do not aggregate a minimum of One Thousand Dollars ($1,000.00) which shall be due and payable by Kutol to B & D on or before December 31, 1963, and annually thereafter, Kutol shall make up the deficiency of the actual royalties paid to such minimum sum.

(i) It is agreed that no royalties shall be paid to B & D until a mechanical patent application is filed in the United States, but that upon the notification of such filing all royalties which have accrued from past sales shall be paid with the next succeeding monthly report.

(j) Kutol shall require every party sub-licensed by Kutol in the United States or foreign countries to guarantee that the annual royalty paid to B & D under the sub-license shall not be less than $500.00. Each sub-license shall contain a royalty schedule as set forth in VI (f) herein.

VII. RECORDS

Kutol agrees to keep records showing the sales of Extrusion Devices sold or otherwise disposed of under the license herein granted in sufficient detail to enable the royalties payable hereunder by Kutol to be determined, and further agrees to permit its books and records to be examined during ordinary business hours from time to time for the purpose only and only to the extent necessary to verify the reports provided for in paragraphs (a) and (b) of Article VI, such examination to be made at the expense of B & D by an independent auditor appointed by B & D who shall report only the amount of royalty due and payable.

VII. NO IMPLIED RIGHTS

Without limiting the grants provided in Article IV above, no rights are granted or implied by this agreement under any patents other than those which shall be issued on or as a result of the application or applications referred to in Article II of this agreement.

IX. NOMENCLATURE

Kutol agrees to inform B & D promptly after the execution of this agreement as to the specific nomenclature and type designation under which Kutol will render bills covering sales of Extrusion Devices under the rights herein granted, and further agrees to inform B & D of any change or new designations which may thereafter be made or adapted to such presses, and Kutol in rendering bills for Extrusion Devices sold under the rights herein granted, agrees that it will in such bills invariably use the nomenclature and type designation so furnished to B & D.

X. ADMISSION OF VALIDITY

If a patent or patents are issued pursuant to Article II above, Kutol will admit the validity of said letters patent under which rights herein are granted thereto, and will agree

that it will not during the term of this agreement directly or indirectly attack or question the same, but such admission of validity is limited to the scope of the rights granted and to the term of this agreement.

XI. ASSIGNABILITY

(a) The obligations of Kutol hereunder, including the obligations to make reports and pay royalties, shall run in favor of the successors, assigns, or other legal representatives of B & D.

(b) Kutol's rights under this agreement and the license herein granted shall pass to any assigns for the benefit of creditors of Kutol and to any receiver of its assets, or to any person or corporation succeeding to its business in the Extruder Device as a result of sale, consolidation, reorganization, or otherwise, and Kutol shall have the right to grant sublicenses, provided that such assignee, receiver, sublicensee, person or corporation shall accept in writing the provisions of this agreement and agree to become in all respects bound thereby, but may not be otherwise transferred without the written consent of B & D. The failure of an assignee to so accept the terms of this agreement shall result in the termination of this agreement and the failure of a sub-licensee to so accept the terms of this agreement shall result in the termination of the sub-license.

Termination under this paragraph can be effected only as follows: if within 60 days following the transfer of rights as provided above B & D has not received an acceptance of the terms of this agreement, B & D shall give Kutol or its assignee notice by registered mail of the failure to accept. This agreement or the sub-license, whichever is applicable, shall be automatically terminated if the terms of this agreement are not accepted within 30 days of such notice.

XII. PROSECUTION OF UNLICENSED COMPETITION

In the event during the existence of this agreement there is any infringement by others of any patents granted on the applications or inventions herein licensed or agreed to be licensed to Kutol, it is agreed that Kutol shall have the sole right to proceed against such infringers. Upon notification to B & D thirty (30) days prior to filing such suit or taking other action as Kutol may deem advisable, Kutol may require B & D to participate in the yearly expenses of such suit or involved action to a maximum of 50% of the yearly expense involved or to the extent of the royalties paid to B & D during the preceeding calendar year, whichever is less. The proceeds of any damages that may be recovered as the result of such suits shall be shared in the same proportion as the expenses incurred by B & D and Kutol in the prosecution of such suits.

It is further agreed that, if after 30 days notice from B & D to Kutol that a party is infringing any of said patents, Kutol fails to bring suit against the infringing party, B & D may, at its option, take appropriate action, including suit, against such infringing party; and any monies recovered through B & D's sole action shall be the property of B & D.

XIII. TERMINATION

(a) If Kutol shall at any time default in the payment of any royalty or making of any report hereunder, or shall commit any breach of any covenant herein contained, or shall make any false report and shall fail to remedy any such default, breach or report within thirty (30) days after written notice thereof by B & D, at its option, B & D may terminate this agreement and the rights herein granted by notice in writing to such effect.

(b) At any time after one (1) year from the date of this agreement, Kutol shall have the right to terminate this agreement at the end of any calendar year, provided there is no default hereunder, by written notice given to B & D at least thirty (30) days prior to the end of such year. In the event that this agreement is brought to an end, either by termina-

tion, cancellation, discharge, or otherwise at the election of Kutol or upon or as a result of a breach of Kutol, Kutol agrees that it will not thereafter engage in the business of manufacturing or selling Extrusion Devices within the field or scope of this agreement as provided in Article I.

Following termination Kutol may reinstate this agreement by giving sixty (60) days notice to B & D provided that Kutol pays the minimum royalties which went unpaid during the period following termination and that the percentage basis for future royalty payments be based on a total of sales which includes the number Extrusion Devices sold while Kutol was previously operating under this agreement; and provided further that B & D has not entered into any contract, with a third party having exclusive provisions which would preclude Kutol's reinstating this contract. B & D agrees that it will not make any contract with a third party which would prevent Kutol's manufacture of Extrusion Devices after the normal expiration of this contract.

(c) In the event that Kutol shall demonstrate the existence of unlicensed competition materially interfering with its business hereunder, and the party or parties hereto are unable or unwilling to prevent or restrain such unlicensed competition, Kutol shall have the right to terminate this agreement and its license hereunder by written notice given to B & D at least thirty (30) days prior to such termination.

(d) Unless previously terminated in accordance with the foregoing provisions of this Article XIII, this agreement and the rights granted hereunder shall run to the full end of the term or terms of any Letters Patent that may issue on or as a result of the application or applications referred to in Article II hereof or for a period of 25 years, whichever is longer, and shall thereupon terminate.

XIV. PATENT INFRINGEMENT SEARCH

Licensors shall promptly, within thirty (30) days after the execution of this Agreement, cause a patent infringement search to be made by a reputable patent law firm in order to determine whether the within described Extrusion Device in its manufacturing, using, or selling would constitute an infringement on a previously issued patent. Upon the completion of such patent infringement search, the Licensors shall forthwith submit to Licensee the written professional opinion of such patent law firm which opinion shall advise as to the likelihood and/or probability that the manufacturing, using, and selling of said Extrusion Device would constitute an infringement of prior Letters Patent. The cost of such patent infringement search shall be borne equally by the Licensors and by the Licensee.

XV. LAW THAT GOVERNS

This agreement shall be construed in accordance with the law of the State of Ohio insofar as such law is existent or applicable and can or will be applied in the jurisdiction in which either party may seek adjudication of any such matter.

XVI. NOTICE

All notices provided for in this agreement shall be given in writing and may be served either by personal delivery or by depositing the same, postage prepaid, in the United States Registered Mails adressed to to parties respectively at the following addresses:

Kutol Products, Inc.
2815 Highland Avenue
Cincinnati 12, Ohio

Robert Boggild
5463 Hill & Dale Drive
Cincinnati 13, Ohio

or

William L. Dale
197 Ireland Ave.
Cincinnati 18, Ohio

or to such other address or addresses as Kutol or B & D respectively may later fix by written notice to the other.

XVII. LIABILITY

Kutol agrees to hold B & D harmless from any claims which arise by virtue of failure of materials or workmanship used in the production of Extrusion Devices covered by this agreement.

XVIII. MODIFICATION

This agreement is the entire and only agreement between the parties, and it supersedes all pre-existing agreements between such parties, respecting the subject matter hereof, and any representation, promise or condition in connection therewith and not incorporated herein shall not be binding upon either party. No modification, extension, waiver, and no termination of this agreement or any of the provisions herein contained shall be binding upon the party against whom enforcement of such modification, renewal, extension, waiver or termination is sought, unless made in writing and signed by the parties, or in the case of Kutol Products, Inc., by one of its executive officers. As used herein, the word "termination" includes any and all means of bringing to an end prior to its expiration by its own terms this agreement, or any provision thereof, whether by release, discharge, abandonment or otherwise.

IN TESTIMONY WHEREOF, the said Kutol Products, Inc., has caused its corporate seal to be hereunto affixed and duly attested and these presents to be signed by its proper of-

ficer hereunto duly authorized, and the said Robert Boggild and William L. Dale have hereunto set their hands.

KUTOL PRODUCTS, INC.

Witness: /s/ _____ By /s/ _____

(Title) (Seal)

Witness: /s/ _____ /s/ ROBERT BOGGILD

Witness: /s/ _____ /s/ WILLIAM L. DALE

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

ROBERT BOGGILD and WILLIAM L. DALE,
Plaintiffs,

vs.

KENNER PRODUCTS, A DIVISION OF
CPG PRODUCTS CORPORATION,
Defendant.

CASE NO. 83-638 (Civil Action)

DEPOSITION OF JOSEPH McVICKER

BE IT REMEMBERED that pursuant to Rule 27(b), and on Thursday, December 19, 1985, commencing at the hour of 9:00 a.m., at Quail Lodge, 8205 Valley Greens Drive, Carmel Valley, California 93923, before me, Joan Mitchell, CSR No. 2569, a Notary Public, personally appeared Joseph McVicker.

APPEARANCES

For Plaintiffs:

Messrs. SANTEN, SHAFFER & HUGHES
Attorneys at Law
105 East Fourth Street, Suite 916
Cincinnati, Ohio 45202
BY: WILLIAM B. SINGER, Esq.

For Defendant:

Messrs. MARSHALL, O'TOOLE, GERSTEIN,
MURRAY & BICKNELL
Attorneys at Law
2 First National Plaza
Chicago, Illinois 60603
BY: MADELINE HENDRICKS DEVEREAUX, Esq.

[1]

JOSEPH McVICKER,

being first duly sworn by the Notary Public to testify to the truth, the whole truth, and nothing but the truth, was examined and testified as follows:

EXAMINATION

BY MR. SINGER:

Q. Would you state your name sir?

A. Joseph Samuel McVicker.

Q. And what's your current address, Mr. McVicker?

A. 722, Carmel, California 93921.

Q. Are you currently employed, or retired, or what?

A. I'm currently doing seminars in England on the entrepreneur, and doing creativity workshops in Carmel.

Q. Just by way of a brief history, as I understand, you are the developer, or inventor, shall we say, of a product called Play-Doh; is that correct?

A. Yes.

Q. Could you, for the benefit — for the Trier of Fact in this case — give us, briefly, how it happened that you were able to develop this product called Play-Doh?

A. Play-Doh came from a product called Wallpaper, one word, Cleaner, which was a flour-based product used in the '40's to clean wallpaper inexpensively in the Midwest where there were lots of walls and dirt — Ohio, Illinois, et cetera, Pittsburgh.

[2] On the back of the can, it said, "Use as a modeling compound," but nobody ever did, and in 1955 I decided to do

that. And to do that, I changed the product and made it non-toxic, made it smell like cookies, and put it in pretty primary colors and went out to market it for the kids.

Q. And did you — during the course of your marketing, did your marketing efforts meet with some success?

A. Yes.

Q. And I'm talking now, initially, about a period prior to the time when you began to sell plastic toys along with it. Did you achieve a substantial success in the marketing of Play-Doh?

A. Yes, I think so. Yes, I mean I don't know, how do you define that? Sales were $31,000 the first three months, and I think 230 the next six months, and two million the next months.

Q. And as far as the product — strike that. What you are talking about in terms of the sales is the product Play-Doh alone; is that correct?

A. I was only in the bulk tonnage business of sellng a single toy, Play-Doh. Whatever facilitated that was okay.

Q. Okay.

A. And different packages. There was a three-pack, a four-pack. There were giant cans. Any way to sell [3] Play-Doh.

Q. Did you find that after the initial period of success in marketing Play-Doh that you needed something else to help sell Play-Doh, something to go with it?

MS. DEVEREAUX: I object to the leading nature of the question. I think Mr. McVicker is capable of answering his own questions in his own words.

BY MR. SINGER:

Q. Let me see. For purposes of argument, I'll accept that and we'll go and try to rephrase the question.

Mr. McVicker, did you, after initial success, find that you wanted something else to go with the marketing of Play-Doh?

A. Yes.

Q. And what was that?

A. Anything which would sell more Play-Doh. Cookie cutters, extrusion devices, merchandising ideas.

Q. Okay.

A. Play-Doh — there was a need for Play-Doh. It would be real nice to take credit for being a genius, but the fact is there was a basic need for this product with young preschool children. It was clean and safe, and it was inexpensive, and mothers made it at home for years.

Q. I. see.

A. But you have it all wrapped up in nice, pretty colors, [4] smelling good, for — then, 59 cents for four cans — something that was easier than making it at home and it didn't get sticky. So there was a lot of success because the need was already there. And we filled the purpose.

Q. How did you first come up with the idea of marketing toys along with Play-Doh?

A. I wanted to sell all the product I could, and there was a lot of pressure on the toy business so that things were — like the Hula Hoop — were fads. There were very few staples. Monopoly was one of them. But we had only been there three years, '55. By '58 the toy industry said, quote, "Look, you are going to be a fad and you are going to go out of business unless you add toys," and I said, "I want to sell Play-Doh." I said, "Find me things that use that product." That's how it worked.

Q. Okay. Now, how is it that you got involved with Boggild and Dale, what was the purpose of that association in the beginning?

A. They came to me to sell an idea for a toy which would use Play-Doh, and they came to my office in Norwood, N-o-r-w-o-o-d —

Q. Norwood, Ohio?

A. Yes, sorry.

Q. And what did they offer you at that time? What was [5] the idea?

A. They had an extrusion device that looked like a red schoolhouse called the Fun Factory. It wasn't called anything. They had an extrusion device with a plunger and configuration that looked like a schoolhouse, and interchangeable dies, and by putting the Play-Doh in the schoolhouse and

pumping the handle, you were able to extrude it like an old-fashioned cookie cutter. And the idea had a lot of appeal to me, so I went to work to make a deal.

Q. And you initially entered into a license agreement with the particular extrusion device; is that correct?

A. Yes.

Q. Now, let me just ask you in general, with respect to your relationship with Boggild and Dale, how were they to be compensated for any ideas that they would come up with?

A. We made a contract to pay them a royalty on every device sold.

Q. Did you ever —

A. It was a comprehensive agreement.

Q. Did you ever pay them just to come up with ideas?

A. No, no. My idea was that I'm doing you a favor and you are helping me, but I've got to take the risk of putting this out on the market; and, therefore, this is what I want you to do, in the contract.

[6] Q. In terms of the development of ideas, in terms of engineering and things of that nature, would they ever be paid for just those services?

A. No. My idea was a flat royalty with a graduated basis based on how many units are sold, and for this contract, you have to do the following: You try to get whatever legal protection you can. You render all the technical assistance that you can because I'm a marketer. I don't know how to do this and I don't want to be messing with dies and molds and plastic, and so part of your deal with me is you are going to have to take care of all that and you've got to be available for emergencies if I'm in England or someplace and, say, the handle's broken. You've got to fix it.

Q. I see. Now, the initial Fun Factory that you mentioned — and let me back up a minute. You began to identify the extrusion device that looked like a schoolhouse, as the Fun Factory. Is that the name that it finally was marketed under?

A. Yes, it was marketed as the Fun Factory.

Q. Okay.

A. There was a later one, a smaller version that was called the Fun Factory, Jr.

Q. That's what I wanted to get to. From that initial Fun Factory device then, there was a later evolution [7] to a smaller device called the Fun Factory, Jr.; am I right?

A. Yes.

Q. And would you describe the Fun Factory, Jr. — and by the way, I might indicate that that is the particular device that is the subject matter of this litigation —

A. The first one was larger, and while it had great appeal to me, the second one was smaller and less expensive at retail. I don't know, maybe $3.00 versus five. It had — I thought I could sell more of them because it was less expensive and it was less cumbersome. It was a technical improvement. Instead of a plunger and separate parts, you had it all in one handle. Isn't that the way it worked? It's been a long time.

Q. Was it safer for children to use?

A. Oh, yes, much easier, and you didn't break handles. The technical aspect didn't cause me any problems and increased the market.

Q. Did — I guess at some point Mr. Boggild and Mr. Dale brought you the idea for the Fun Factory, Jr.?

A. All the ideas for the toys were brought to me.

Q. And did they disclose it to you in confidence?

A. I think — I think after the first one, I had a bad experience. I had signed a confidential disclosure several years before with a man named Marvin Glass, [8] on an extrusion device to use Play-Doh. When he heard of the Fun Factory, he sued me for violation, and he lost. So I was careful about words like that.

Q. Okay. In any event, they disclosed this device?

A. They brought it — I think they came into my office with their idea and I liked it and bought it and made the agreement. And they did the same thing with the Fun Factory, Jr.

Q. We're talking now about the Fun Factory, Jr., when they brought it to you?

A. They brought it to me.

Q. Did you like the device?

A. Yes.

Q. And did you want to market it?

A. Yes.

Q. Okay. What — Let me show you what's been marked as Plaintiff's Exhibit Number 1, Mr. McVicker, and ask you if you can recognize what that is a copy of.

A. Yes, this is an agreement between Boggild and Dale and Kutol, K-u-t-o-l, Products.

Q. What is Kutol Products?

A. It was the manufacturing company — Rainbow Crafts was the marketing company, and Kutol was the manufacturing company. I own both of them.

Q. Kutol was the company that manufactured —

A. They were effective financial tools for me to have [9] two companies.

Q. But Kutol was the company which manufactured Play-Doh?

A. Yes. So the agreement was between Kutol and Boggild.

Q. If you look on the last page of this Exhibit 1, you see a copy of your signature there?

A. I do.

Q. All right. In terms of the provisions of this agreement, did you negotiate those provisions with Messrs. Boggild and Dale?

A. Yes. Primarily with Bob Boggild when Dale was present, but Boggild and I did most of the working out of the agreement.

Q. What role, if any, did attorneys play in negotiations and the formation of agreements?

A. My attorneys were Taft, Stennins & Hollister, and they approved the contract and got any terms — you know, they wrote up — I think his attorney and mine, but they didn't have anything to answer specifically. The didn't have anything to do with negotiations.

When I made the deal I wanted with Boggild, I asked them

to translate it legally and to check with his attorney if it was okay. The attorneys gave legal approbation, that's all.

Q. What was your object in negotiating this agreement with Boggild and Dale? What was your objective?

[10] A. Sell Play-Doh.

Q. I see. And —

A. And make money, you know, but they were the same to me.

Q. Let me ask you whether or not the patent protection, or the potential of patent protection, played a significant role in your negotiations?

MS. DEVEREAUX: I object to the extent that I don't understand what you mean by "significant." Obviously, if Mr. McVicker understands what you mean by it, he's free to answer whatever he understands.

BY MR. SINGER:

Q. Let me rephrase the question, Mr. McVicker. The agreement contains certain provisions with respect to patent and patent applications. Given that, can you tell us what, if any, role the expectation that a patent might issue for this device played in your willingness to pay royalties for the use of the device?

A. That's a long question. Please rephrase it simply for me.

Q. Let me try.

Did the likelihood that this device would be patented affect your desire to pay royalties for it?

A. No, I couldn't wait for that. That patent process is lengthy, and, I think, fairly worthless. It took me nine years to get a patent on Play-Doh. I don't [11] know how long it took to get a Fun Factory, Jr., patent, but if I waited for that, someone else may have invented a toy to take its place or — so, I went out and marketed — I went out and sold it to Toy Fair by January. By March, I had this in all the toy catalogs.

Q. When did you have — did you have any idea when you signed that agreement, that this toy was going to be patented?

A. I didn't know, I certainly asked, after this bad experience that I had if I would be protected any way I could be protected, and they should at least see if they could get a patent protection, and protection is an additive, but it's not determinative for me. What determines it is, can I sell it, and can I get it to the market first?

Q. Did the likelihood or the expectation that patents would issue for this device in any way affect your willingness to pay royalties for a term of at least 25 years?

A. Say it again so I can answer the question.

Q. The period of this agreement, as it's stated in — let me see if I can find it.

Okay. On Page 14 of Exhibit 1, the paragraph D, which appears in the middle of that page, if I'm correct, provides for a minimum period of 25 years —

A. That's right.

[12] Q. — of the royalty obligation.

A. Right.

Q. Did the thought that this device may be patentable influence, in any way, your desire to pay royalties for the use of the device and to pay those royalties for that period of time?

A. The patent and the application and the assertion of the patent, and the possible issuance of a patent, did not determine my making a deal with Boggild. What determined it was a whole package, which included their giving me technical and manufacturing assistance, solving manufacturing problems, taking responsibility to search infringement, the cost of filing for an application and seeing it through without any cost or liability to me; and that's the deal I made with them.

Q. In general, Mr. McVicker, what had your experience been, prior to 1963, with respect to the efficacy of the patent protection?

A. I didn't have a patent on Play-Doh. I filed it in '55 or '56 and I got in in '64, and under duress from my employees to get protection. I think the only protection is marketing dominence. If you are there, where somebody else isn't; if the patent comes along, it's an additive and it's a nice one, but it's

not to be depended upon to make a [13] profit or to market the product.

Q. Okay.

A. It is a potential protection, but only potential, depending on the intricacies of the patent law and the skill of the inventor in convincing the patent office of its uniqueness.

Q. Did you, during the course of time that your patent application was pending for Play-Doh, have occasion to deal with competitors in that product?

A. Yes.

Q. And how —

A. I had two competitors, one product called Kid-Dough, in Cleveland, Ohio, and another called Fun-Dough in St. Louis. They were both produced by manufacturers of wallpaper cleaners, which is what we were originally, and they were older gentlemen and they both tried to compete unsuccessfully.

Q. How did you achieve your dominence in that product —

A. Marketing.

Q. — briefly?

A. Marketing. By putting it in the schools — I'll tell you how.

I went to New York City with a can of Play-Doh in my hand, and walked into NBC and walked up to whatever floor — to the Ding-Dong School, which was [14] before Captain Kangaroo, which — who's been on longer than Nixon — and walked onto the set and said, "Here, I've got this great product," and somehow the woman, Dr. Horowitz, accepted it — Miss Frances — and then I got calls from agents saying, "You can't do that. You've got to have a contract and you've got to pay royalties," and whatever; so I made a contract in Beverly Hills, California, for what I had already done in New York, and paid five percent in order to have national exposure on national television; and that's the thing I did.

Another thing was going to schools and convincing the school teachers they could have free Play-Doh for these poor kids. Another was getting the Parents Seal of Approval.

Another was buying television spots in Evansville, Indiana. Another was going to England in 1957, when I didn't have distribution in the Midwest; but I was going to put this all over the world. That was my idea.

Q. I take it from the fact that during this period of time you did not have patents, that patents did not contribute, or the potential patentability did not have —

MS. DEVEREAUX: Objection, leading.

BY MR. SINGER:

Q. Let me ask you, Mr. McVicker — I'll rephrase the [15] question.

THE WITNESS: I agree with you.

MR. SINGER: I agree with her, too.

THE WITNESS: I agree with you.

BY MR. SINGER:

Q. I didn't do that deliberately, but sometimes we fall into that.

Did the patentability, or not, or the existence of patents or not, with respect to Play-Doh, in any way add to or detract from its marketing success?

A. Potentially added to. Potentially added to say "Patent Applied For," but in actuality it didn't do anything until the patent was issued. So the promise of a patent was not the equivalent to having a good patent issued. The potential — I mean we didn't have anything. The reason the Fun Factory sold is because we put it out there with a good product. The reason we put the next one out is because the first one sold, and we were smarter, and on the next one, there was a contract patent search, and infringement and protection were part of the total contract all along, and of more importance to me was technical stuff, assistance. And even more important to me, as I'm sitting here, having read it again this morning, I hedged my bet by graduating the royalties.

Q. I see. Let me ask you about that. The agreement [16] provides that royalties — let's get the exact provision.

Again on Page 6 of the Exhibit 1, Paragraph 6F(1) provides for graduated royalties. What was your idea in providing for graduated royalties at that time?

A. I wanted the minimum risk and the minimum cost because the cost of marketing a product was substantial and I wanted to see if the product was substantial and I wanted to see if the product would sell. I wanted to — I wanted Boggild and Dale to be cooperative and not create problems, but facilitate my objectives, which was to put a can of Play-Doh in every kid's hand in the world.

Q. In terms of, then, the graduation of the royalties, the agreement does not say that the graduation of royalties, the increase of royalties, the percentage of royalties, is contingent upon the issuance, or not, of a patent?

Let me ask whether or not that's consistent with your view of the importance of patents in this negotiation process?

MS. DEVEREAUX: I object to the question. I don't understand it at all and I don't know how you would intend to use it if you ever got the opportunity. And I'm — so I don't know what the meaning of any answer to that he's going to give, would be, because [17] I truly cannot understand the question.

MR. SINGER: Well, then, let me just ask Mr. McVicker to answer the question if he understands it.

THE WITNESS: Could you read it back?

BY MR. SINGER:

Q. Let me rephrase it, because I think it was perhaps a bit clouded.

In agreeing to graduated royalties, was it the increase in sales that influenced your willingness to pay a higher royalty rate?

MS. DEVEREAUX: I still object. I mean, why don't you ask him what it was that influenced his willingness to pay a higher royalty rate, instead of trying to put words and suggestions in his mouth?

MR. SINGER: I'll take your suggestion.

BY MR. SINGER:

Q. What was it, Mr. McVicker, that influenced you to agree to increase the royalty rate? What was it that it was contingent upon?

A. Success.

Q. Okay. Did patent have anything to do with it?

A. Patents were simply applied for. They weren't issued.

Q. Okay.

A. I'm not acquainted with what your legal arguments are about. I'm saying the Fun Factory helped sell [18] Play-Doh. I wanted to minimize what I was paying, until I could perceive that it was a good item. I was quite willing, when I had made my sales of the Fun Factory, to share; but I was asking with the initial outlay of designs, molds, marketing, if they would minimize — obviously I was saying, "Hey, you trust me, I'm a good marketer. If I make money, you'll make money." And they bought that and, you know, that was part of the contract, and all they said is, "Listen, can we have at least a thousand dollars a year?" or something. There was some minimum. I don't remember whether it was $10,000 or $1,000. Okay. There was some minimum, and since I had no development costs, since I didn't have to do anything but dial 911 to get the hotline if I had a problem, since they were going to apply for a patent infringement so I wouldn't get sued by Marvin Glass again for confidential disclosure, that was the whole package, and, based on a trend — am I allowed to tell a story off the record?

A man jumped out of the 32nd floor of the Empire State Building. At the 31st floor, he passed a man at a window of the Empire State Building, who said, "How is it going?" He said, "So far, so good, but the trend is bad."

Now, the trend of the Fun Factory was good; [19] therefore, I was willing to pay, based on the trend.

Q. All right. Mr. McVicker, when you — it's in the patent infringement search, and there is a provision to this agreement that provides that there should be a patent infringement search?

A. Right.

Q. Let me ask you whether or not that — well, strike that.

Let me ask you very simply, what was the purpose, from your point of view, of having a patent infringement search with respect to this device?

A. I wanted everything I could get. I wanted protection, if I could get it. I wanted the — no liability. Remember, I'd been in a lawsuit over a confidential disclosure on an extrusion device, and I didn't want to do that again. I didn't want to get into any legal liability. It's quite similar to the — asking for my deposition and that's fine with me that this is on the record.

Q. What I'm saying to you is asking you your — was it your purpose in wanting a patent infringement search to determine whether or not this product would be patentable, or was it to determine whether or not, if you marketed the device, you would get potentially sued by somebody else who claimed the device?.

A. I think it's both. I can't separate them. It was [20] to protect me from liability and it was to add to my success with the Fun Factory if we could get a patent.

Q. Did the —

A. The momentum was not created by the patent. It was created by the market, but I asked for everything I could get in the market, minimal cost, technical assistance, patent search, patent application.

Q. Okay. Well, let's talk about, then — specifically with reference to the royalty terms, Mr. McVicker. In negotiating the royalty terms, did you assume any degree of likelihood that valid patents would issue?

A. Did I assume that?

Q. In other words, did you have any — let's make it simpler.

Did you have any idea whether or not patents would issue at the time you negotiated?

A. No, I didn't know that.

Q. Okay. Did it — in terms of your willingness to pay the royalties, all right, did whether or not patents issued affect your willingness to pay royalties?

A. No.

Q. Did whether or not patents issued affect your willingness to pay royalties for a minimum twenty-five year term?

A. No. I made a deal to sell this toy. I made a contract.

[21] Q. Now, Mr. McVicker, let me draw your attention to Article VI G, Good, of the agreement, which is on Page 7, and ask you whether or not that paragraph expresses in this agreement what you have just testified to?

A. Yeah, it's agreed that we pay whether the filing happens or not. That's what it says here.

MR. SINGER: All right. That's all the questions I have, Mr. McVicker.

You may cross-examine.

EXAMINATION

BY MS. DEVEREAUX:

Q. Mr. McVicker, I would like for you to look at the paragraph that begins at the bottom of Page 13, in the small c — with a small c, Article 13 of the contract.

Have you had an opportunity to read it?

A. Yeah, I have.

Q. All right. Now, as I understand, as I read that language at least, that provides that in the event you experienced unlicensed competition that was affecting your business, I take it that's the business of selling the Fun Factory, Jr., that the parties were unwilling or unable to prevent or restrain, you had the right to terminate the agreement?

A. That's right. That's what it says.

[22] Q. Do you understand why that provision was included in the agreement.

A. I understand why I included it.

Q. Why is that?

A. I included it because I didn't want them to sell it to somebody else. I wanted to be the source of it.

Q. Was exclusivity in selling important to you then?

A. The maximum protection, and certainly the major part of that was being the only manufacturer of this item — that was part of it.

I'm talking about an exclusive right to sell.

Q. Did you —

MR. SINGER: Excuse me. The witness is explaining his answer and he hasn't finished his answer.

THE WITNESS: I'm just saying I had a — is this a debate, Counselor? — exclusive right to sell, is what I wanted.

MS. DEVEREAUX: I wasn't intending to interrupt the witness and I resent your implication that I was. It's my understanding that he paused and was finished. I'm sorry.

BY MS. DEVEREAUX:

Q. Did you understand at that time that an issue of patent would give you the right to exclude others from selling the Fun Factory, Jr.?

A. I didn't have any confidence, Mrs. Devereaux, in [23] patents, but I tried to apply for one. I did not know when and if they would issue and how — how strong and how willing I would be to defend them if they did issue. I asked for everything. I asked for all the legal protection I could get and I asked for Boggild and Dale not to diffuse my efforts in marketing by having other people market the product. I mean, if tires were an exclusive, it would be an incredible monopoly, you know. If one company, Goodyear, Goodrich or somebody, were only able to make tires, it would change their position.

Q. All right.

A. To at least not to have to compete with other people on the same toy could help my position, and to apply for a patent was — patent was one of the ways to help do that; but it was not the only way.

MS. DEVEREAUX: I have no further questions.

MR. SINGER: Nor do I.

Thank you Mr. McVicker. Thank you Counsel.

WITNESS

[Jurat Omitted]

PD -900. , "PLAY-DOH" FUN FACTORY, JR. . SUGG. RET. $2.00 (OR LESS) - FASCINATING FUN FACTORY, JR. EXTRUDING TOY OF DURABLE CYCOLAC PLASTIC WITH 3 NEW "MINEATURE" 2-OZ. CANS OF PLAY-DOH. TWO SLIDE-THRU DIE-STRIPS WITH 10 DIFFERENT MODELING DESIGNS FOR HOURS OF FUN. TRIMMER AND ILLUSTRATED BOOKLET. FULL VIEW VISUAL PACKAGE FOR EASY DISPLAY. (12 TO SHIPPER; WT. 15 LBS.) RAINBOW CRAFTS, INC. CINCINNATI 12, OHIO.

No. 85-1579

Supreme Court, U.S.
FILED
MAY 28 1986
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CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

ROBERT BOGGILD and WILLIAM L. DALE,
Petitioners,

v.

KENNER PRODUCTS, A Division of
CPG PRODUCTS CORP.,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

BRIEF OF KENNER PRODUCTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

Whether the Court of Appeals correctly applied *Brulotte* v. *Thys Co.*, 379 U.S. 29 (1964) in holding that the *Brulotte* rule of *per se* invalidity precludes enforcement of license provisions which were developed in anticipation of patent protection and which require royalty payments for sale of a patented item beyond the life of the patent at the same rate as was required prior to expiration of the patent.

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IN THE

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CPG PRODUCTS CORP.,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

BRIEF OF KENNER PRODUCTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

This brief is filed by Respondent, Kenner Products,[1] in response to the Court's request of May 16, 1986. Kenner

[1] As indicated in Respondent's letter to the Court dated April 7, 1986, the entity that was previously known as CPG Products Corp., including all of its operating divisions, was spun-off by its former parent, General Mills, Inc., to the shareholders of General Mills on November 1, 1985 under the name Kenner Parker Toys Inc. Hence, Kenner Products is now an operating division of Kenner Parker Toys Inc. and, at least for the present purposes, Kenner Parker Toys Inc. is successor to the named Respondent, CPG Products Corp.

respectfully submits that the decision of the United States Court of Appeals for the Sixth Circuit, reported at 776 F.2d 1315, is in full accord with this Court's holding in *Brulotte v. Thys Co.*, 379 U.S. 29 (1964), with all other Supreme Court authority cited by the Petitioners, and with the Eleventh Circuit's recent decision in *Pitney Bowes, Inc. v. Mestre,* 701 F.2d 1365 (11th Cir. 1983), *cert. denied,* 464 U.S. 893 (1983), a case which is indistinguishable from the present case. Accordingly, the present petition for writ of certiorari should be denied.

STATEMENT OF THE CASE

The facts necessary for this Court's review of the present petition are found in the underlying contract of this action and in the patents that issued to Petitioners, Boggild and Dale, pursuant to the requirements of the contract.[2] Pertinent aspects are, for the most part, set forth in the opinion of the Court of Appeals and will not be dwelled upon here. 776 F.2d at 1316-1317. However, in view of Petitioners' insistence upon characterizing the underlying contract as a "trade secret" agreement, and their concomitant avoidance of various key provisions of the contract, certain of its provisions warrant attention.

First, it is noted that the words "trade secret" do not even appear in the four corners of the contract. Article II of the agreement contains the unambiguous requirement, however, that both design and mechanical patent applications be filed to cover the licensed extruder device. Specifically, Article II, entitled "Patent Applications," provides:

> "B & D will promptly file and diligently prosecute at their expense both mechanical and design patent appli-

[2] The agreement is included in the appendix to the Boggild and Dale Petition for a Writ of Certiorari, pages 27a-38a. The patents, U.S. Patent No. Des. 200,480 and U.S. Patent No. 3,264,685, are included in the Supplemental Appendix to the Boggild and Dale Petition.

cations directed to said Extrusion Device in the United States and Canada.

* * * *

"It is agreed that if B & D fails to file the patent applications in the United States and foreign countries specified above Kutol shall have the right to file the said applications and to deduct the costs of such filing from royalty payments owed to B & D."[3]

Boggild and Dale applied for both design and mechanical patents to cover the licensed extruder device in the United States, as *required* by Article II of the agreement, and critical to this case, *both patents issued.* The design patent expired March 2, 1979; the mechanical patent August 9, 1983.

The issuance of patents pursuant to the Article II application requirements, and thus the licensing of patent rights, was anticipated by numerous provisions of the agreement. For instance, Article IV grants the *exclusive* right to manufacture, use, and sell the licensed extruder; Article X provides that Kenner will admit the validity of any "patent under which rights herein are granted;" Article XII gives Kenner the right to enforce "any patents granted on the applications or inventions herein licensed;" and subparagraph (c) of Article XIII gives Kenner the right to terminate the license in the event of unlicensed competition which the parties "are unable or unwilling to prevent or restrain."

The important aspect of the agreement which both Petitioners and the Amicus Association ignore is that the *only* basis for payment to Boggild and Dale is the Article VI provision for payment of royalties on sales of the licensed device. Specifically, there is no provision in the agreement for payment based on "trade secret" or "technical service" items, as erroneously implied in Petitioners' first question presented for review and

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[3] Kutol is a predecessor in interest under the contract to Kenner. *See* 776 F.2d at 1316 n.1.

also in the brief of the Amicus Association. (*See, e.g.,* Amicus Brief, page 5). Indeed, there is no provision anywhere in the agreement for payments to Boggild and Dale for any reason other than the Article VI provision for payment of royalties on sales of the extruder, *i.e.,* the patented subject matter.

Finally, at the heart of the Sixth Circuit's unenforceability decision is Article XIII, subparagraph (d), which provides:

> "Unless previously terminated in accordance with the foregoing provisions of this Article XIII, this agreement and the rights hereunder shall run to the end of the term or terms of any Letters Patent that may issue on or as a result of the application or applications referred to in Article II hereof or for a period of 25 years, whichever is longer, and shall thereupon terminate."

It is this provision that causes the agreement to run afoul of this Court's holding in *Brulotte v. Thys Co.*, 379 U.S. 29 (1964), and it is also this provision that makes this case indistinguishable from the Eleventh Circuit's decision in *Pitney Bowes, Inc. v. Mestre,* 701 F.2d 1365 (11th Cir. 1983), *cert. denied,* 464 U.S. 893 (1983). In providing for the payment of royalties to extend beyond the full term of the lawful monopoly of the patents, based on post-expiration sales and payable at the same rate and on the same basis as for pre-expiration sales, the contract term is in clear violation of federal patent policy.

REASONS FOR DENYING THE PETITION

I. THERE IS NO CONFLICT NOR CONFUSION CAUSED BY THE SIXTH CIRCUIT OPINION

Both Boggild and Dale and the Amicus Association assert that the Sixth Circuit's application of the *Brulotte* rule of *per se* invalidity in this case is in conflict with prior decisions of this Court, and that the Sixth Circuit opinion creates confusion in this area of intellectual property law. (*See, e.g.,* Petition, pages 10-11; Motion for Leave to File Amicus Curiae, page 2).

Kenner submits, however, that the Sixth Circuit opinion is in full accord with all precedent cited by both the Petitioners and the Association. As discussed in more detail below, the clearly established line of demarcation in all of these cases rests upon the *issuance* of patents vis-a-vis the *absence* of patent rights, and this line of demarcation derives directly from and is reflective of the *public* interests inherent in the granting of a patent monopoly.

Kenner further submits that rather than causing confusion, the Sixth Circuit's opinion removed the only confusing conflict that existed when it reversed the district court opinion below. (Reported at 576 F.Supp. 533). In declining to follow *Brulotte,* the district court expressly declared itself to be in conflict with the Eleventh Circuit by finding that that court had "over extended the *Brulotte* rule" in its *Pitney Bowes* decision. 576 F.Supp. at 536-37. Thus, the Sixth Circuit opinion that is the subject of the present petition removed all conflict and confusion.

A. Application of Brulotte Is Consistent with and Supported by the Public Interest Inherent in a Patent Grant

Review of the present petition must begin with an understanding of the philosophy underlying the federal patent grant. It is a fundamental tenet of United States patent law that an

inventor is provided a seventeen-year monopoly to his discovery in exchange for his disclosure of it to the public. At the end of the seventeen-year period, the law provides that his exclusive rights in his discovery expire and the invention enters the public domain. *Scott Paper Co. v. Marcalus Manufacturing Co.*, 326 U.S. 249, 255-57 (1945); *Brulotte v. Thys Co.*, 379 U.S. 29, 30-31 (1964); *Lear, Inc. v. Adkins*, 395 U.S. 653, 673-74 (1969); *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 480-81 (1974).

The philosophy behind the patent grant demands consideration of the rights of the public, not merely those of the parties to a particular patent agreement. As Chief Justice Stone stated in *Scott Paper Co.*:

> "... The nature and extent of the legal consequences of the expiration of a patent are Federal questions, the answers to which are to be derived from the patent laws and the policies which they adopt. [citations omitted]. By the patent laws Congress has given to the inventor opportunity to secure the material rewards for his invention for a limited time on condition that he make full disclosure for the benefit of the public of the manner of making and using the invention, and that upon expiration of the patent the public be left free to use the invention. [citation omitted]. As has been many times pointed out, the means adopted by Congress of promoting the progress of science and the arts is the limited grant of the patent monopoly in return for the full disclosure of the patented invention and its dedication to the public on the expiration of the patent. [citations omitted].
>
> "The aim of the patent laws is not only that members of the public shall be free to manufacture the product or employ the process disclosed by the expired patent, *but also that the consuming public at large shall receive the benefits of the unrestricted exploitation, by others, of its disclosures.* [citation omitted]. *If a manufacturer or user*

> *could restrict himself by express contract,* or by any action which would give rise to an 'estoppel,' *from using the invention of an expired patent, he would deprive himself and the consuming public of the advantage to be derived from his free use of :he disclosures.* The public has invested in such free use by the grant of a monopoly to the patentee for a limited time. *Hence any attempted reservation or continuation in the patentee or those claiming under him of the patent monopoly after the patent expires, whatever the legal device employed, runs counter to the policy and purpose of the patent laws."* 326 U.S. at 255-56 (emphasis added).

As evident from the foregoing, the grant of a patent is intended to be a *quid pro quo* agreement between an inventor and the public at large. By its grant of the patent, the public bestows upon the patentee the right to exclude all others from making, using and selling his invention for a period of seventeen years. The public is thus deprived of the "unrestricted exploitation, by others" throughout the patent's term. Exploitation, either by manufacturing, selling or using the invention himself or by licensing any of these rights to others, lies in the sole discretion of the patentee. This is the price the public pays for the Constitutionally sanctioned encouragement of invention.

In return for such rigorous statutory protection, the patentee owes allegiance to the public. Most importantly, after expiration of the patent, the public is entitled to a free market with respect to the patented subject matter, *i.e.,* a market no longer encumbered by financial tribute to the expired patent monopoly. Hence, Chief Justice Stone continued in his *Scott Paper* analysis:

> "By the force of the patent laws not only is the invention of a patent dedicated to the public upon its expiration, but the public thereby becomes entitled to share in the goodwill which the patentee has built up in the patented article or product through the enjoyment of his patent monopoly.
>
> * * * *

> "It is apparent that the patent laws preclude the patentee of an expired patent and all others including petitioner from recapturing any part of the former patent monopoly; for those laws dedicate to all the public the ideas and inventions embodied in an expired patent. *They do not contemplate that anyone by contract or any form of private arrangement may withhold from the public the use of an invention for which the public has paid by its grant of a monopoly and which has been appropriated to the use of all. The rights in the invention are then no longer subject to private barter, sale, or waiver." 326 U.S. at 256-57 (emphasis added).*

See also Brulotte v. Thys Co., 379 U.S. 29, 31-32 (1964); *Lear, Inc. v. Adkins*, 395 U.S. 653, 673-74 (1969).

Thus, in *Scott Paper*, this Court set out a concise and coherent analysis of the public's rights in inventions for which the patent grant has expired. The Court held in *Scott Paper* that no private individual would be permitted to abridge the public's rights by agreeing to extensions of the patent monopoly. The key holding in *Scott Paper* was that "any attempted reservation or continuation in the patentee ... of the patent monopoly, after the patent expires, whatever the legal device employed, runs counter to the policy and purpose of the patent laws." 326 U.S. at 256.

Kenner submits that the Sixth Circuit's opinion is fully consistent with and supported by the underlying public interest in the patent grant, as expressed so well by the Court in the *Scott Paper* analysis. The present petition must be reviewed in light of the clear federal policy favoring free public access to the inventions disclosed in expired patents.

B. The Sixth Circuit Opinion Is Consistent with and Supported by the Scope of Brulotte v. Thys

In *Scott Paper*, the holding was that an alleged infringer could not be barred from practicing the teachings found in expired patents. *Scott Paper* did not involve an attempt to

collect royalties beyond the life of a licensed patent, but it set out the principles which would later be relied upon by the Court to bar such an attempt. *Brulotte v. Thys Co.*, 379 U.S. 29, 30 (1964).

In *Brulotte*, the Court applied the *Scott Paper* principles to strike down a license agreement which required the licensees to continue paying royalties based on post-expiration conduct after expiration of the patents involved. The holding was that such an agreement was unlawful *per se*.

The material facts underlying the holding in *Brulotte* were simple: (1) the hop-picking machines, which were sold for a fixed price, were covered by a number of U.S. patents; (2) licenses to use the inventions covered by the patents and incorporated into the machines were granted with the sale of the machines and required annual royalty payments separate from the fixed sale price of the machines; (3) royalties were exacted for the licensed use, based alternatively on a minimum annual payment or on pounds of hops picked per season; (4) all applicable patents expired in 1957, but the royalty payment obligations continued for terms beyond that date; and (5) the royalty rates in question were based on post-expiration use of the machines and were at the same rate as for pre-expiration use.

In these circumstances, the Court held that:

> "The exaction of royalties for use of a machine after the patent has expired is an assertion of monopoly power in the post expiration period when, as we have seen, the patent has entered the public domain. We share the views of the Court of Appeals in ArTik Systems v. Dairy Queen, Inc., 302 F.2d 496, 510 ... that after expiration of the last of the patents incorporated in the machines 'the grant of patent monopoly was spent' and that an attempt to project it into another term by continuation of the licensing agreement is unenforceable." 379 U.S. at 33-34.

In reaching its holding in *Brulotte,* the Court expressly rejected arguments that the royalty payments were for something *other* than the grant of rights under the patent, finding it "peculiarly significant" that the machines in issue were *patented* articles and that the royalties (1) were specifically based on post-expiration usage, and (2) were at the same rate and payable on the same bases as for pre-expiration usage. 379 U.S. at 31-32. These considerations were stated by the Court to:

> "... forcefully negate the suggestion that we have here a bare arrangement for a sale or a lease at an undetermined price, based on use. The sale or lease of *unpatented* machines on long-term payments based on a deferred purchase price or on use would present wholly different considerations. ... But patents are in the federal domain; and 'whatever the legal device employed' [citation omitted] a projection of the patent monopoly after the patent expires is not enforceable." 379 U.S. at 32 (emphasis in original).

In *Brulotte,* the Court found the license contracts to be "on their face a bald attempt to exact the same terms and conditions for the period after the patents have expired as they do for the monopoly period." 379 U.S. at 32. Thus, the Court was not interested in conjecturing "what the bargaining position of the parties might have been and what resultant arrangements might have emerged had the provision for post-expiration royalties been divorced from the patent and nowise subject to its leverage." 379 U.S. at 33.

Kenner submits that the scope of *Brulotte* is as follows: where a license agreement provides for the payment of royalties on the manufacture, use, or sale of subject matter which is patented, and the agreement, on its face, provides for the payment of royalties after expiration of the applicable patents, based on post-expiration activities, at the same rate and payable on the same basis as for pre-expiration activities, the

agreement is unlawful *per se* and it is unenforceable beyond the expiration date of the patents. In such circumstances, the courts may not look to the equities of the parties, or who drafted the license, or what role the patents played in fact in the negotiation of the license agreement, inasmuch as such conjecture regarding the motives, "leverage power," and "bargaining positions," of private parties has no place in determining the fundamental interests of the public when issued patents are involved. *See Scott Paper Co. v. Marcalus Manufacturing Co.*, 326 U.S. 249, 255-57 (1945). The violation apparent on the face of the agreement is considered so contrary to established federal policy that no attempt to justify it will be permitted. That is the import of any *per se* rule, and it applies to the *Brulotte* holding as well as any other.

C. Application of Brulotte in the Present Case Is Consistent with and Supported by this Court's Prior Holdings in Kewanee and Aronson

In arguing that the Sixth Circuit has "confused" the law and is in conflict with decisions of this Court, both Boggild and Dale and the Amicus Association rely on two Supreme Court cases wherein the respective holdings specifically turned on the fact that *no* issued patents were involved: *Kewanee Oil Company v. Bicron Corporation,* 416 U.S. 470 (1974) and *Aronson v. Quick Point Pencil Co.,* 440 U.S. 257 (1979). (See, *e.g.,* Petition, pages 10-11; Amicus Brief, pages 10-11, 14). Kenner submits, however, that the Sixth Circuit's application of *Brulotte* in this case, where patents *did issue,* is also consistent with and supported by these cases.

Kewanee was an action based upon employment agreements requiring the non-disclosure of confidential information or trade secrets obtained as employees. The holder of the trade secrets sought injunctive relief and damages for the misappropriation of its trade secrets by certain of its former employees. The employees argued that federal preemption prevented enforcement of the non-disclosure agreements inasmuch as the claimed trade secrets included matter that could

have been, but was not patented. The trade secret owner in *Kewanee* had never applied for any patents, opting instead to rely on state trade secret protection. Thus, the question before the Court in that case was whether the *alternative* protection of state trade secret law was available to one who had intentionally and unequivocally forgone the protections of the federal patent laws. See 416 U.S. at 483-84. After reviewing the respective objectives and alternative incentives of *both* methods, Chief Justice Burger stated,

> "Certainly the patent policy of encouraging invention is not disturbed by the existence of *another* form of incentive to invention. *In this respect* the two systems are not and never would be in conflict. *Similarly, the policy that matter once in the public domain must remain in the public domain is not incompatible with the existence of trade secret protection. By definition a trade secret has not been placed in the public domain."* 416 U.S. at 484 (emphasis added).

The above-quoted passage starkly illustrates the fallacy of Boggild and Dale's assertion that the agreement herein should be treated as a "trade secret" license and also to the error in Petitioners' and the Amicus Association's suggestions that the Sixth Circuit's opinion will serve to discourage inventors from filing patent applications. (Petition, page 10; Amicus Brief, page 14). First, just as a trade secret "by definition" has not been placed in the public domain, a patent "by definition" is public. Its disclosures are published upon issuance, and upon expiration become the property of the public by law. *See* Section IA, *supra.* Thus, when Boggild and Dale agreed to file patent applications, thereby necessarily publishing their disclosure upon issuance of the patents, Boggild and Dale *chose* the federal patent laws as their means of protection, thereby foregoing the "alternative" protection at issue in *Kewanee.*

With respect to the suggestions that patent applications will be discouraged, one need only read the entirety of the

Chief Justice's opinion in *Kewanee.* One who chooses to protect his inventions with the "far weaker" state trade secret laws is always at "substantial risk" that his discoveries will be learned by someone else through legitimate means, *e.g.,* independent discovery or reverse engineering. 416 U.S. at 489-90. In that event, the trade secret owner is not entitled to receive royalties for or to prohibit any such unlicensed competition. *See also Sears, Roebuck & Co. v. Stiffel Co.,* 376 U.S. 225, 230-31 (1964); *Compco Corp. v. Day-Brite Lighting, Inc.,* 376 U.S. 234, 237-38 (1964). On the other hand, one who obtains valid patent protection for his inventions receives the publicly granted right, for a term of seventeen years, to exclude *all* others from making, using, and selling the invention throughout the United States. 35 U.S.C. § 154. As the Chief Justice recognized in *Kewanee,* the patent laws of the U.S. operate " 'against the world,' forbidding any use of the invention for whatever purpose for a significant length of time." 416 U.S. at 490.

Thus, *Kewanee* clearly is not inconsistent with the Sixth Circuit's holding in this case. In any event, since there were no issued patents involved in *Kewanee,* the Court was not faced with the ultimate question decided by the Sixth Circuit here, *viz.,* whether an agreement that provides for the payment of royalties on the manufacture, use or sale of subject matter which was covered by expired United States patents may be enforced beyond the expiration of those patents, where the royalties would be payable on post-expiration activities, at the same rate and on the same basis as for pre-expiration activities. The only Supreme Court cases that have addressed this issue are *Brulotte v. Thys Co.,* 379 U.S. 29, 32 (1964) and ironically, the other case relied upon by the Petitioners and the Amicus Association, *Aronson.* Kenner submits that the Sixth Circuit opinion is also consistent with, and indeed supported by, the holding and the analysis applied by this Court in that case.

Aronson involved a royalty agreement covering rights in a new keyholder designed by Mrs. Aronson and licensed to Quick

Point. Mrs. Aronson had applied for, but had not obtained, patents on the keyholder at the time the agreement was first entered into. In the words of Chief Justice Burger:

> "The contract was embodied in two documents. In the first, a letter from Quick Point to Mrs. Aronson, Quick Point agreed to pay Mrs. Aronson a royalty of 5% of the selling price in return for '*the exclusive right to make and sell* keyholders of the type shown in your application. Serial No. 542677 ....'
>
> "... Quick Point retained the right to cancel the agreement whenever 'the volume of sales does not meet our expectations.' *The duration of the agreement was not otherwise prescribed.*
>
> "A contemporaneous document provided that *if Mrs. Aronson's patent application was 'not allowed within five (5) years,* Quick Point Pencil Co. [would] pay ... two and one half percent (2½%) of sales ... so long as you [Quick Point] continue to sell same.' " 440 U.S. at 259 (emphasis added).

No patents issued within the five-year time period (or thereafter). Hence, Quick Point reduced the amount of its royalty in accordance with the "no patent" contingency provision of the second part of its agreement, and continued paying royalties to Mrs. Aronson at the 2½% rate for an additional fourteen years.

Quick Point then filed an action seeking a declaratory judgment that the agreement was unenforceable on the ground that state contract law, which might otherwise make the contract enforceable, was preempted by federal law. The agreement was upheld by the district court. The Eighth Circuit reversed, finding that the federal patent policy favoring the full and free use of ideas in the public domain required that Quick Point be relieved of its obligations to Mrs. Aronson. *Quick Point Pencil Co. v. Aronson,* 567 F.2d 757, 760-762 (8th Cir. 1977). The court of appeals further observed that had Mrs. Aronson been successful in obtaining a patent on her keyholder, "under *Brulotte v. Thys Co., supra,* 379 U.S. at 32, Quick Point's

liability for royalties would have ended after seventeen years *in spite of the contract."* 567 F.2d at 762 (emphasis in original).

The Eighth Circuit opinion was reversed by this Court, the Court finding that state contract law was not preempted by federal patent law *where no federally issued patents are involved.* However, in the course of analyzing the facts of that case in light of the *Brulotte* holding, the Chief Justice specifically noted the court of appeals' conclusion regarding the application of *Brulotte* to the contract in issue, stating:

> "The [appellate] court also observed that if Mrs. Aronson actually had obtained a patent, Quick Point would have escaped its royalty obligations either if the patent were held to be invalid, [citation omitted] or upon its expiration after 17 years, see *Brulotte v. Thys Co.,* 379 U.S. 29 (1964)." 440 U.S. at 261.

Even though the Supreme Court reversed the lower court on the facts in *Aronson,* where no patent had issued, the Chief Justice expressly agreed with the court of appeals regarding the issue decided by the Sixth Circuit in this case, stating:

> "Mrs. Aronson attempted to obtain a patent for over five years. *It is quite true that had she succeeded, she would have received a 5% royalty only on keyholders sold during the 17-year life of the patent."* 440 U.S. at 263-64 (emphasis added).

In their petition, Boggild and Dale speculate that in making these statements, the Chief Justice may have merely been commenting "on the terms of the contract." (Petition, page 18). The error in Boggild and Dale's conjecture is that it overlooks the fact that the duration of the 5% provision in the *Aronson* agreement is *not* expressly limited to the life of any patent. As quoted above, the duration of the agreement was "not prescribed."

Kenner submits that what the *Aronson dicta* represents is a recognition by the Court that had a patent issued, the unlawful *per se* rule of *Brulotte* would have been controlling regardless of the fact that no patent had issued prior to the negotiation of the license, despite the lack of evidence of any coercive leverage applied, and without concern for any "advantage" Quick Point may have gained by being the "first in the marketplace." (See Petition, pages 22-23). This is true because had a patent issued, the public would have paid its price via the grant given to Mrs. Aronson to exclude others from exploiting her invention. Since Mrs. Aronson's patent application was denied, the public had never paid its price, *i.e.,* it had never been deprived of the "unrestricted exploitation, by others" of Mrs. Aronson's keyholders. *See Scott Paper Co. v. Marcalus Manufacturing Co.,* 326 U.S. 249, 255-57 (1945).

The contract provision that was enforced in *Aronson* was for a *reduced* royalty that rested expressly on the *contingency* that no patent issue. Since no patent issued, the market for the keyholders designed by Mrs. Aronson had always been free, and there was no public interest reason for finding the contingency provision unenforceable. Kenner submits that, contrary to Petitioners' assertion, the Sixth Circuit opinion is supported by both the holding and the dicta of *Aronson.*

D. The Sixth Circuit Opinion Is Consistent with and Supported by Every Other Lower Court Opinion Addressing the Issue

As indicated above, Kenner submits that the present case is indistinguishable from the Eleventh Circuit's recent decision in *Pitney Bowes, Inc. v. Mestre,* 701 F.2d 1365 (11th Cir. 1983), *cert. denied,* 464 U.S. 893 (1983). Indeed, the reasoning of the

Eleventh Circuit was relied upon by the Sixth Circuit in reaching their decision here.[4]

Pitney Bowes represents a step closer to the present case than *Brulotte* in that it dealt with a factual situation wherein the patents involved did not exist at the time the agreements were entered into but did later issue. In *Pitney Bowes,* at the time the agreements were entered into the patent applications had been filed, but there was no way of knowing whether the patents would ever issue.[5]

The court in *Pitney Bowes* had no hesitation in applying *Brulotte* as controlling, because the patents had in fact issued; the patents covered the licensed subject matter; the obligation to pay royalties, on the face of the agreement, extended beyond the life of the patents; the post-expiration royalties were based on post-expiration activities; and there was no differentiation between the pre- and post-expiration royalty rates.

Thus, as in the present case, the royalties in *Pitney Bowes* were not tied to any particular patents or patent applications. The royalties were due on the various machines, whether they were patented or unpatented. Further, neither the grants of exclusive rights nor the royalty requirements included any distinction between the lives of patents that might issue and post-expiration periods. Also as in the present case, while none

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[4] It is noted that although the Amicus Association argues that the Sixth Circuit opinion will cause "confusion," it did not even cite the one circuit court decision factually indistinct from the Sixth Circuit opinion, *i.e., Pitney Bowes.* This omission appears particularly inexcusable in view of the Sixth Circuit's express reliance upon its sister court's decision.

[5] Boggild and Dale have never asserted that there is any materiality in the fact that in *Pitney Bowes* the patent applications had been filed at the time the agreement was executed, whereas here the applications were filed after execution of the agreement. This undoubtedly is because the present agreement *required* the filing of the patent applications.

of the agreements were contingent upon patents issuing, patents did in fact issue with respect to all four of the agreements involved sometime after each of the respective agreements went into effect.

The Florida district court found that of the four basic agreements, the first agreement was strictly a trade secret license (*but see* 701 F.2d at 1373 n. 13) while the latter three agreements were "hybrid" agreements, expressly licensing both patent and trade secret rights. As expressed by the district court, "The principle issues to be decided with respect to all four amended agreements are what are the expiration dates of the agreements and what are the post expiration consequences." 517 F.Supp. 52, 59.

The issue as to expiration of the agreements in *Pitney Bowes* arose from the same sort of violative contract provisions regarding their respective terms as that found in Article XIII(d) of the contract in the instant case. For instance, the second *Pitney Bowes* contract, termed the "Vertical Collator Agreement," was entered into in 1959 and provided for the expiration on the date of Mestre's death, on the date of expiration of the last U.S. patent to expire, or after seventeen years, *whichever was latest.* Since Mestre lived for more than the seventeen-year period and past the expiration of the last to expire patent, the issue before that court regarding the enforceability of a royalty agreement after expiration of the applicable patents was directly on point with the issue decided by the Sixth Circuit in this case.

Relying on the same Supreme Court authority that Boggild and Dale assert in their petition, *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257 (1979) and *Kewanee Oil Company v. Bicron Corporation*, 416 U.S. 470 (1974), Mestre argued that because of the portion of the "hybrid" agreements that provided for rights under the trade secrets, *Brulotte* was inapplicable, and that the trade secret portion of the agreement warranted the

continuation of royalty payments throughout the express terms provided in the contracts, despite the expiration of the patents.

The Eleventh Circuit thus analyzed the terms of the Vertical Collator Agreement in accordance with the same authority asserted before the Court in the present petition. In its analysis, that court of appeals found two aspects of the Agreement particularly analogous to the misuse found to be unlawful in *Brulotte*: (1) the conditions of the grant of exclusive use were identical both before and after the patent rights expired, and (2) the royalty terms were identical both before and after expiration of the patents and included no allocation for royalties paid under the patent rights versus rights under the trade secrets. The court stated:

> "... As in Brulotte, two provisions in the [Vertical Collator] agreement suggest that the patentee used the leverage of his patent to project its monopoly beyond the 17-year patent period. First, the 'exclusive rights' granted under the agreement applied equally before and after expiration of the patent. Like the assignment and removal restrictions on the hop-picking machines in Brulotte, the grant of exclusive rights is 'pertinent to protection of the patent monopoly,' but its applicability to the post-expiration period is a telltale sign that the licensor was using the license to project its monopoly beyond the patent period.' 379 U.S. at 32, 85 S.Ct. at 179. Second, the agreement required Pitney Bowes to pay royalties at the same rate and on the same basis after the patent expired that it paid while the patent was in effect. Assuming that the value of the agreement to Pitney Bowes was not as high after the patents expired, it is reasonable to assume that at least some part of the post-expiration payment constituted an effort to extend payments for patent rights beyond the patent period." 701 F.2d at 1373.

The court concluded that pursuant to the clear mandate of *Brulotte*, the Vertical Collator Agreement was unenforceable upon the date of expiration of the last involved patent to expire, even though that contract specifically provided for the licens-

ing of trade secret rights in addition to "any" patents which "may issue," even though the payment of royalties was not contingent upon any patents ever issuing, and even though the contract expressly provided for the payment of royalties for a term beyond the expiration of the last patent to expire.

In granting Pitney Bowes' motion for summary judgment with respect to this contract, the Florida district court concluded that,

> "... the extension of the obligation to make royalty payments, pursuant to the Vertical Collator Agreement, beyond the expiration of the underlying patents represents too great an encroachment on the federal patent system." 517 F.Supp. at 63; this part of the of district court opinion *aff'd*, 701 F.2d at 1370-73.

The "encroachment" that the district court in *Pitney Bowes* was referring to is an encroachment of the *public's* interest in the federal patent system, as discussed in Section IA, *supra*. Kenner submits that the Eleventh Circuit opinion and all other lower court decisions known to Kenner that deal with the issues involved in the Petition support the Sixth Circuit's holding that the critical factors to application of *Brulotte* are (1) whether or not patents *did* issue covering the subject matter of the agreement and (2) whether enforcement of the agreement would require payment of royalties after expiration of the applicable patents, based on post-expiration activities, and at the same rate and on the same basis as before the patents expired. *See, e.g., Meehan v. PPG Industries, Inc.*, No. 84 C 6967, slip op. at 6a-9a (N.D. Ill. July 3, 1985), *argued*, No. 85-2495 (7th Cir. April 11, 1986);[6] *Rocform Corp. v. Acitelli-Standard Concrete Wall, Inc.*, 237 F.Supp. 34, 41-44 (E.D. Mich. 1964), *aff'd*, 367 F.2d 678, 680 (6th Cir. 1966); *Prestole Corp. v. Tinnerman Products, Inc.*, 271 F.2d 146, 155 (6th Cir. 1959); *Pipkin v. FMC Corporation*, 427 F.2d 353, 357 (5th Cir. 1970); *Outman et al.*

[6] A copy of the unpublished district court opinion is included in the appendix hereto, pages 1a through 9a.

v. Western Contracting Corp., 204 U.S.P.Q. 289, 291-92 (N.D. Iowa 1979); and *Veltman v. Norton Simon, Inc.*, 425 F.Supp. 774, 775 (S.D.N.Y. 1977).

In fact, Kenner has been unable to find any case where a patentee has been allowed to continue to collect royalties for sales of *patented* subject matter after expiration or invalidation of his patents, *unless* the payments were expressly allocated against something other than the patented subject matter. Indeed, the cases cited by Petitioners, *Chromalloy American Corp. v. Fischmann*, 716 F.2d 683, 686 (9th Cir. 1983) (sellor of patent license, related know-how, and business assets limited to compensation for "non-patent" assets after patent found invalid); *Span-Deck, Inc. v. Fab-Con, Inc.*, 677 F.2d 1237, 1247 (8th Cir. 1982), *cert. denied*, 459 U.S. 981 (1982) (entire royalty under contract held avoidable after patents held invalid because no allocation of percentage of royalties attributable to trade secrets and know-how provided); and *St. Regis Paper Co. v. Royal Industries*, 552 F.2d 309, 315 (9th Cir. 1977), *cert. denied*, 434 U.S. 996 (1977) (licensor not entitled to royalties under license agreement after patent held invalid inasmuch as patent rights and know-how "intimately intertwined" and agreement did not distinguish between royalties payable for each) (Petition, page 20 n.2), are exemplary of Kenner's position, and certainly not in conflict with the Sixth Circuit opinion here inasmuch as the underlying contract in this action makes *no* allocation between patented subject matter and surviving "trade secrets." (*See*, pages 3-4, *supra*).

Thus, while both the Petitioners and the Amicus Association assert that the Sixth Circuit opinion is in conflict with other cases and will cause confusion among the bar, neither of these parties has pointed to a single case that withstands analysis. Kenner submits that because the Sixth Circuit opinion is in fact in full accord with this Court's holding in *Brulotte v. Thys Co.*, 379 U.S. 29 (1964), as well as with all of the

remaining Supreme Court and lower court authority cited by the Petitioners and the Amicus Association, there is no basis for the grant of a writ of *certiorari* in this case. Accordingly, the Boggild and Dale petition should be denied.

II. THE SIXTH CIRCUIT DID NOT MAKE FINDINGS OF FACT, BUT MERELY APPLIED THE LAW OF BRULOTTE TO THE ONLY RELEVANT AND UNDISPUTABLE FACTS OF RECORD—THE CONTRACT ITSELF AND THE EXPIRED PATENTS

Petitioners' second question presented for review asserts that the Court of Appeals improperly made findings of fact concerning the parties' use of potential patent leverage. This assertion is premised on both a misunderstanding of a *per se* rule and a mischaracterization of the Sixth Circuit's opinion.

First, application of the *Brulotte* rule of *per se* invalidity means that it is not necessary to reach the factual question of whether there was "leveraging" of the patent monopoly. Kenner submits that such inquiries were expressly precluded by the Court's creation of the *per se* rule of *Brulotte*. Thus, the Court said that when the fact of the extension of the monopoly is apparent from the face of the agreement (as it is here), it did not want to "conjecture" as to what the bargaining position of the parties might have been. Indeed, the Court stated that if such devices were available to patentees, "the free market visualized for the post-expiration period would be subject to monopoly influences that have no proper place there." 379 U.S. at 32-33. In short, it is not relevant whether the potential patent was intentionally "leveraged" or whether the licensee considered himself to be subject to patent "leverage." What is clear and determinative is that the patent *was* extended beyond its terms, to the *public's* detriment, by the contract in question, and that is what *Brulotte* guards against with its *per se* rule.

Second, Kenner submits that the Sixth Circuit did not make improper "findings of fact." Rather, it applied the *per se* rule of *Brulotte* to the only relevant and undisputable facts of record—the contract itself and Petitioners' expired patents. The Sixth Circuit first presented a thorough analysis of *Brulotte,* and concluded that portion of its opinion with its ultimate holding:

> "We reverse [the district court] judgment and hold that the *Brulotte* rule of *per se* invalidity precludes enforcement of license provisions which were developed in anticipation of patent protection and which require royalty payments for use, sale or manufacture of a patented item beyond the life of the patent." 776 F.2d at 1319.

The court then included a *dictum* discussion of the leveraging analysis in the Eleventh Circuit's *Pitney Bowes* decision, and concluded that the terms of Petitioners' contract also evidenced leveraging. The *dictum* is in no way necessary to support the holding, as is clear from the passage quoted above.[7]

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[7] It is noted that Petitioner has attached the transcript of a deposition of the original licensee, taken after the appeal was decided, in an attempt to show "no leverage." Surely such extra-record material has no place in the petition. Nevertheless, Kenner submits that the transcript exemplifies the wisdom of the *per se* rule. Not only is the testimony, taken 23 years after the fact, confusing and inconclusive, but more importantly it shows that the public interest must not be held hostage to the narrow interests of private parties evidenced by that transcript.

CONCLUSION

For the foregoing reasons, Respondent respectfully requests that the petition for a writ of certiorari be denied.

KENNER PRODUCTS, A Division
of CPG PRODUCTS CORP.,

By_____

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APPENDIX

IN THE UNITED STATES DISTRICT COURT

For The Northern District Of Illinois

Eastern Division

JOHN C. MEEHAN,

Plaintiff,

-vs-

PPG INDUSTRIES, INC.,

Defendant.

No. 84 C 6967

MEMORANDUM OPINION AND ORDER

John C. Meehan (Meehan) brought this diversity action for breach of contract against PPG Industries, Inc. (PPG). In 1964, Meehan assigned an invention to PPG's predecessor-in-interest. PPG paid Meehan royalties pursuant to the contract until the U.S. patent covering the invention expired in January, 1983. The case is before the court on cross-motions for summary judgment.

I. Factual Background

The following facts are largely undisputed. In the early 1960's, Meehan, a salesman for a plumbing and heating supply company, conceived an anti-icing additive for private aircraft engines. In 1963, Meehan attempted to market his so-called "method and apparatus" for packaging and dispensing his invention. One of the chemical companies he contacted, Hoffman-Taff, Inc., the predecessor corporation of PPG, expressed interest in the market potential of Meehan's invention.[1]

After PPG signed a confidentiality agreement, Meehan disclosed his invention to it. By the end of December, 1963, Meehan had orally agreed to sell all rights and interests in his

[1] For the purposes of simplification, the contract will be considered as one between Meehan and PPG.

invention to PPG. Accordingly, on January 30, 1964, the parties executed a written contract of assignment.

> Under the contract, Meehan agreed to
>
> sell, assign and transfer unto [PPG] ... the full and exclusive right to apply for and obtain ... patents or other like protection ... for ... the ... method and apparatus covered by this contract in the United States and all foreign countries ... and all the right and authority ... to make, use, manufacture and vend the ... method and apparatus ....

Exhibit "A" to Complaint at ¶ 2. In exchange for this exclusive assignment, PPG contracted to pay Meehan a variable sum of royalties on sales "derived from selling or otherwise utilizing" the method and apparatus. *Id.* at ¶ 3. The parties' cross-motions revolve around the interpretation of the following provision:

> The payments above provided for shall be payable by [PPG] to MEEHAN for a period of time not to exceed the life of any patent or patents granted upon the method and apparatus covered by this contract, and if no patent is granted, for a period of time not to exceed ten (10) years from the date of this contract.

Id. at ¶ 6.

On the contract date, Meehan had not filed any patent application for his invention. The contract, however, obligated PPG to immediately "determine whether the method and apparatus ... may be patented, and if, in the sole judgment of [PPG] and its attorneys, such method and apparatus may be patented, then [PPG] shall file and prosecute with diligence an application for United States Letters Patent ...." *Id.* at ¶ 8(a). In this connection, Meehan assented to render such technical assistance, furnish all available information, and execute all documents necessary for the purpose of applying for and successfully prosecuting a patent application. *Id.* at ¶¶ 8(b), 10. If patents issued, the contract provided that Meehan "shall

. . . legally and completely assign, transfer and convey to [PPG] said Letters Patent." *Id.* at ¶ 8(b).

Pursuant to the contract, patents covering Meehan's invention were applied for and granted in the U.S., Canada, and the United Kingdom. The U.S. patent (No. 3,227,196) issued on January 4, 1966 and expired on January 4, 1983. The British patent lapsed without renewal on November 11, 1981. Finally, the Canadian patent (No. 773,811) did not expire until December 19, 1984. The contract neither segregates royalty payments according to these patents nor differentiates between the rate of such payments before and after expiration of the patents.

PPG paid Meehan royalties under the contract until January 4, 1983, when the U.S. patent expired. Since that date, PPG has made sales in the U.S. deriving from Meehan's invention but has made no further royalty payments.

Meehan sued for breach of contract in 1984. Under his construction of the contract, PPG was obligated to pay royalties until the last of the U.S. or foreign patents expired. Thus, plaintiff argues that he was entitled to royalties through December 19, 1984, when the Canadian patent expired. Citing *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257 (1979), plaintiff insists that 1) he contracted to sell nothing more than a trade secret and, therefore, 2) the term of the contract is enforceable as written under applicable state law.[2]

In contrast, PPG asserts that its obligation to pay royalties to Meehan ceased on January 4, 1983 as a matter of federal patent law. PPG does not dispute Meehan's interpretation of the contract language that the agreement was to remain in effect through the life of the last-to-expire patent. Rather, PPG argues that plaintiff's construction would improperly extend the

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[2] The contract is expressly governed by Missouri law. Exhibit "A" to Complaint at ¶ 19.

obligation to pay royalties on sales of the patented invention for nearly two years after the expiration of the U.S. patent. PPG invokes *Brulotte v. Thys Co.*, 379 U.S. 29 (1964) for the proposition that such an extension is unlawful *per se*, state contract law to the contrary notwithstanding.

Because this case presents a pure question of law, summary judgment is an appropriate vehicle for adjudication. Summary judgment shall be granted only if "there is no genuine issue as to any material fact and . . . the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c).

II. Discussion

In *Brulotte v. Thys Co.*, 379 U.S. 29 (1964), the Supreme Court considered the effect of a license agreement which provided for the payment of royalties beyond the life of the underlying patents. The Supreme Court held that "a patentee's use of a royalty agreement that projects beyond the expiration date of the patent is unlawful *per se*." 379 U.S. at 32. Noting that federal patent rights become public property once the 17-year period of protection ends, the Court emphasized that, " 'whatever the legal device employed'[,] a projection of the patent monopoly after the patent expires is not enforceable." *Id.* (quoting *Scott Paper Co. v. Marcalus Manufacturing Co.*, 326 U.S. 249, 256 (1945)). The Court refused to permit a patentee to misuse the leverage of the patent monopoly in this manner. *Id.* at 33. In addition, the Court found it "peculiarly significant" that the royalty provisions in the agreement at issue were the same for the post-expiration period as for the monopoly period. *Id.* at 31-32. PPG argues that *Brulotte* controls this case.

On the other hand, in *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257 (1979), relied on by plaintiff, the Supreme Court addressed the issue "whether federal patent law pre-empts state contract law so as to preclude enforcement of a contract to pay royalties to a patent applicant, on sales of articles embodying

the putative invention, for so long as the contracting party sells them, if a patent is not granted." 440 U.S. at 258-59. While a patent application was pending, Mrs. Aronson contracted for the manufacture and sale of her invention of keyholders. The contract expressly provided that if a patent was not granted, the royalty payments would be reduced by 50%. *Id.* at 259. After reviewing the policies of federal patent law, the Supreme Court upheld the enforcement of the contract for the sale of what it considered to be a generic trade secret.[3] *Id.* at 262-63; *see also Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470 (1974). The manufacturer's obligation to make continuing royalty payments was viewed as a reasonable *quid pro quo* for the privilege of introducing a new product to the market. *Id.* at 263.

The Court stressed, however, that Mrs. Aronson failed to obtain a patent. The Court noted that "[i]t is quite true that had she succeeded, she would have received a . . . royalty only on keyholders sold during the 17-year life of patent." *Id.* at 263-64. Furthermore, attempting to reconcile its holding with that of *Brulotte*, the Court stated that "[h]ere the reduced royalty which is challenged, far from being negotiated 'with the leverage' of a patent, rested on the contingency that no patent would issue . . . ." *Aronson*, 440 U.S. at 265.

The case at bar starkly illustrates the conclusive effect of legal characterization. *See generally* E. Levi, *An Introduction To Legal Reasoning* 2-3, 5 (1949). If Meehan sold a pure trade secret, then *Aronson* dictates that he receive royalties as contracted for until December 19, 1984. In contrast, if Meehan assigned patent rights, either exclusively or in combination with a trade secret, then *Brulotte* nullifies the contractual obligation to pay royalties after January 4, 1983 as a matter of overriding federal law. After considering all of the materials submitted by the parties, the court concludes that the assignment contract at

[3] The Supreme Court defined trade secret as "confidential information . . . not disclosed in the normal process of exploitation." 440 U.S. at 266 (citing Restatement of Torts § 757 comment b (1939)).

issue and the subsequent events pursuant thereto sufficiently implicate federal patent policy to prohibit the payment of royalties to Meehan beyond the life of the U.S. patent.

First, the face of the contract indicates that Meehan intended to convey and PPG intended to receive much more than a mere trade secret. In addition to the exclusive right to "make, use, manufacture and vend" the invention, Meehan contracted to assign to PPG "the full and exclusive right to apply for and obtain . . . patents or other like protection . . . ." Exhibit "A" to Complaint at ¶ 2. Numerous other provisions show that the parties clearly contemplated the early application for patent protection. *E.g., id.* at ¶¶ 6, 8(a), 8(b), 9, and 10. Indeed, ¶ 8(a) obligated PPG to immediately determine whether the invention was patentable and if, in its judgment, the invention was patentable, then to file and prosecute with diligence a U.S. patent application. Although such a filing is perhaps not mandatory under the imprecise language of this provision, the court recognizes that good faith is an implied term of every contract. *See* Restatement (Second) of Contracts § 205 (1981); *ABA Distributors, Inc. v. Adolph Coors Co.*, 542 F. Supp. 1272, 1285 (W.D. Mo. 1982) (applying Missouri law). In this light, ¶ 8(a) strongly suggests that the parties expected PPG to seek U.S. patent protection at the earliest possible date. Moreover, in the event that a patent issued, ¶ 8(b) explicitly provides that it is the property of PPG. Thus, the court refuses to believe that Meehan innocently negotiated for the sale of a trade secret without the prospect of patent protection.

Second, the contract provides for royalty payments in gross, with no segregation among the various patents issued and no distinction between amounts owing during and after the life of the patents. Unlike Mrs. Aronson, Meehan did not bargain for a reduced payment in the event that no patent issued. Nor did he contract for reduced payments after the expiration of any patents issued. Thus, the contract terms

require the payment of royalties on U.S. sales of the invention occurring after the expiration of the pertinent U.S. patent at the same rate before and after expiration, in contravention of *Brulotte.*

Third, the court declines Meehan's invitation to restrict its inquiry to the intent of the parties on the contract date. The court also weighs the subsequent conduct of the parties pursuant to the contract. The most important fact in this regard is the successful application for patents. This distinguishes *Aronson* and implicates federal patent policy. The constitutionally protected patent monopoly, as well as its concomitant rights and obligations, gives way to the public domain after seventeen years. *See Brulotte,* 379 U.S. at 31; *cf. Aronson,* 440 U.S. at 263-64.

Finally, federal patent policy proscribes the extension of the patent monopoly beyond the life of the patent in this case. Enforcement of the royalty provision until December 19, 1984 would deprive "the consuming public . . . [of] the benefits of the unrestricted exploitation, by others," of Meehan's invention. *Scott Paper,* 326 U.S. at 255. If Meehan's construction were sustained, "the free market visualized for the post-expiration period would be subject to monopoly influences that have no proper place there." *Brulotte,* 379 U.S. at 32-33. There can be little doubt that as long as PPG is obligated to pay royalties to Meehan, the market will not be "free" since the consuming public will ultimately have to bear the burden of PPG's costs as reflected in the price of its product.

Undaunted by these considerations, plaintiff assiduously attempts to distinguish *Brulotte* on the basis that Meehan had not applied for a patent at the time of the contract. It is true that *Brulotte* involved licenses for patents already issued and the improper use of leverage on those patents. The holding in *Brulotte,* however, was not expressly limited to these facts. Furthermore, other courts, in applying *Brulotte* to assignments

of patent rights similar to the contract at issue, have not been detained by the absence of a patent at the time of executing the contract. *E.g., Pitney Bowes, Inc. v. Mestre,* 701 F.2d 1365 (11th Cir.), *cert. denied,* 104 S.Ct. 239 (1983); *Pipkin v. FMC Corp.,* 427 F.2d 353 (5th Cir. 1970); *contra, Boggild v. Kenner Products,* 576 F. Supp. 533 (S.D. Ohio 1983), *argued,* No. 84-3467 (6th Cir. March 26, 1985). Finally, the factors discussed above strongly support the application of *Brulotte* to the facts of this case.

Even assuming *arguendo* that the contract at issue embodies a "hybrid" agreement to sell both a trade secret and patent rights, the court refuses to ignore the patent rights assigned and the federal patent policy arising from the subsequent issuance of patents. The Eleventh Circuit has squarely held that such a hybrid agreement is unenforceable insofar as it requires royalty payments beyond the expiration of U.S. patents. *Pitney Bowes,* 701 F.2d at 1373.[4] Confronted with an issue of characterization like the one before this court, the Eleventh Circuit reasoned that "[w]hen a patent issues, the potential exists for direct conflict between federal patent law and state trade secret law. When such a conflict occurs, the question is . . . one of federal supremacy." 701 F.2d at 1372. In turn, "federal supremacy requires that federal patent law determine the rights under the agreement." *Id.* at 1372 n.12.

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[4] Although not cited by Meehan, one federal court has declined to follow *Pitney Bowes* on similar facts, because, in the court's view, "the Eleventh Circuit over extended [sic] the *Brulotte* rule." *Boggild,* 576 F. Supp. at 536. This court, however, has carefully reviewed both decisions and finds *Boggild* unpersuasive for the following reasons: 1) it ignores the language in *Aronson* indicating that the outcome would have been different had a patent issued; 2) it omits any reference to the fact that the contract in question did not distinguish between the amount of royalties to be paid a) if a patent issued and if no patent issued and b) before and after the expiration of the patent; and 3) it inadequately heeds the federal patent policy of a free market for the post-expiration period.

The court concludes that the issuance of a U.S. patent in this case created a conflict between federal patent law and state trade secret law to be resolved in favor of the former.

III. Conclusion

For the foregoing reasons, the court holds that the royalty provisions of the assignment contract were unenforceable as a matter of overriding federal patent law after January 4, 1983, when the U.S. patent covering plaintiff's invention expired. There being no disputed issue of material fact in this regard, defendant is entitled to judgment as a matter of law. Therefore, the court grants defendant's motion for summary judgment and denies that of plaintiff. The case is dismissed with prejudice.

ENTER:

BERNARD M. DECKER
United States District Judge

DATED: July 3, 1985.

Supreme Court, U.S.
FILED
JUN 5 1986
JOSEPH F. SPANIOL, JR.
CLERK

No. 85-1579

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1985

ROBERT BOGGILD and WILLIAM L. DALE,
Petitioners,

v.

KENNER PRODUCTS, A DIVISION OF
CPG PRODUCTS CORPORATION,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

REPLY BRIEF IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI

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ARGUMENT

Kenner's position (which it says this Court, the Eleventh Circuit and the Sixth Circuit have adopted, ignoring everything this court and those courts have said about misuse of the leverage of a patent monopoly) is simple and direct: whenever a patent exists or comes into being covering any part of the subject matter of a license agreement, royalties are automatically limited to the expiration date of the patent, because, Kenner says, any agreement to pay royalties is *per se* invalid to the extent that the term of the royalty obligation turns out to exceed the life of the patent.

It doesn't take much imagination to perceive the disastrous effects of such a *per se* rule of invalidity upon the market place for new ideas. Any license agreement for unpatented subject matter for which the licensee wants to apply for a patent would become completely uncertain as to its royalty obligation. At the time of negotiating the license agreement, the parties would not know when a patent would issue, if at all. If a patent did not issue, the licensor would clearly be benefitted: having already restricted himself by contract from licensing his invention to others, and having negotiated the best royalty terms he could for all his rights and technical know how in the absence of a patent, he would receive the full benefit of his bargain. Patent issuance, on the other hand, would be a windfall to the licensee, and a disaster to the licensor: If the patent were issued soon enough, the licensee would be relieved of the royalty obligation at the time the patent expired. The longer it took to get the patent issued, the closer the licensor would approach the full realization of his bargain. By diligently prosecuting the patent application, however, the licensor would be digging his own grave. Hence the Kenner/Sixth Circuit *per se* rule encourages delay in the issuance of patents.

Let us look at another example. Assume two parties negotiate a certain royalty for the exchange of technology. The careful lawyer for the licensee asks the licensor if there

are patents that should be licensed under the agreement to be sure that the licensee could practice the technology without infringing such patents. The patents are added, not as a block of rights transferred to enhance licensee's exclusive position, but rather as a safety measure to avoid placing the licensee in the position of infringing the licensor's patents. Under this scenario, a highly likely one, the Kenner/Sixth Circuit *per se* rule would have the agreement expire with the expiration of the patent, regardless of what the parties decided in their negotiations would be an appropriate expiration date.

Suppose an inventor waited to license his invention until he had it patented. In that case, the value of the invention would be limited by an ever-decreasing time period, if the Kenner/Sixth Circuit *per se* rule were the law. If the invention was ahead of its time, or a market did not appear for it until the patent was about to expire, such a *per se* rule would require that the inventor would receive little or no benefit for his disclosure of the invention to the public through the patent process. Indeed, the Kenner/Sixth Circuit *per se* rule would prevent the payment of any royalties beyond the patent expiration date, even if the parties agreed to pay royalties for the invention in installments, rather than lumping royalty payments in the short remaining time of the patent life.

The Kenner/Sixth Circuit *per se* rule would thus transmutate patent protection from a boon intended to encourage the invention and disclosure of new ideas and products, to a trap in which the inventor would find to his dismay that he is powerless to prevent a licensee from reneging on an agreement, fairly negotiated, for the value of his invention.

This Court intended no such result in *Brulotte* v. *Thys Co.*, 379 U.S. 29, 85 S.Ct. 176 (1964). The leverage issue, which Kenner ignores, and which clearly is an issue of fact, was central to this Court's holding in *Brulotte*, as the Court later affirmed in *Aronson* v. *Quick Point Pencil Co.*, 440 U.S. 257, at 264-65, 99 S.Ct. 1096, at 1100 (1979). The unfortunate implications drawn by lower courts from the *per se* language of

the *Brulotte* opinion, however, have led to a series of lower court decisions, including the present one, in which courts have been distracted from the leverage inquiry by the facile attractiveness of a *per se* rule[1]. The full extent of this distraction may not have been apparent to this Court when it denied Certiorari in *Pitney Bowes Inc.* v. *Mestre*, 701 F. 2d 1372 (11th Circuit, 1983), cert. den., 104 S.Ct. 239. But this case has now arisen in the Sixth Circuit, and the Meehan Case[2] is pending in the Seventh Circuit, and the time is ripe for this Court to decide whether freedom of contract or government-sanctioned default will carry the day.

It is significant that every lower court case from *Mestre* to *Boggild* to *Meehan* has relied, in its application of the "*per se*" rule, upon this court's *obiter dicta* in *Aronson* to the effect that if a patent had issued, Mrs. Aronson "would have received a five percent royalty only on key holders sold during the seventeen-year life of the patent." 440 U.S. 257, at 263-64, 99 S.Ct. 1100. Such a use of *dicta* is not only unwarranted; it fairly demands authoritative review and pronouncement by this Court.

Kenner's insistence on the *per se* rule has unwittingly caused it to posit a conflict between the Sixth Circuit Opinion in this case and the Eleventh Circuit Opinion in *Mestre*. If footnote twelve of the *Mestre* opinion (701 F. 2d at 1373) is not to be ignored, the leverage issue is an issue of fact, subject to proof, upon which application of the *Brulotte* rule may turn. Kenner, however, sweeps aside the leverage issue as totally irrelevant, and says that the Sixth Circuit opinion in this case was based solely on Kenner's *per se* rule, incredibly

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[1] At least four members of this Court have recently expressed disfavor of the use of *"per se"* rules, in a concurring opinion in *Jefferson Parish Hospital District No. 2* v. *Hyde*, 446 U.S. 2, 104 S.Ct. 1551, 80 L. Ed. 2d 2 (1984), see the text accompanying footnotes 2 and 7.

[2] *Meehan* v. *PPG Industries Inc.*, No. 84 C 6967 (N.D. Ill. July 3, 1985), appendix to Kenner's brief; the same counsel represent Kenner here and PPG in that case.

dismissing as mere "dictum" the last nine paragraphs of the Sixth Circuit Opinion, in which it unmistakably made findings of fact on the leverage issue. If the Sixth Circuit really meant to expend so much energy on *dictum* — if it really based its decision solely on Kenner's *per se* rule — then its reasoning, if not its result, is in conflict with the Eleventh Circuit in *Mestre*.

Underlying Kenner's reading of the *per se* rule is its assertion that the public interest in a post-patent-expiration free market for patented material prevents the retention by the licensor of any vestige or attribute of the patent monopoly after the patent expires, especially the right to receive royalties from the licensee. Kenner ignores the fact that all members of the public *are* free to practice the invention after the patent expires; only the licensee, Kenner in this case, has to pay royalties to the end of its contract term. In this case, this is a result that Kenner's predecessor freely bargained for and which Kenner did nothing to change when it became the assignee of the license agreement and renegotiated some of its terms in 1970.

Kenner's indulgence in the self-serving fiction that the market freedom of its consuming public is affected by the lingering royalty obligations is simply not worthy of any credence: the retail price of a product is affected by many factors other than costs, including royalties, the most important of which factors is the amount of profit the manufacturer and subsequent dealers think the market will bear. To suggest that the public would enjoy a price reduction if Kenner were relieved of its royalty obligation is disingenuous, if not outright deceitful.

Kenner finds its primary support for its *per se* rule in certain sweeping language contained in this Court's opinion in *Scott Paper Co.* v. *Marcalus Co.*, 326 U.S. 249, 66 S.Ct. 101 (1945). Even though this Court based its decision in *Brulotte* partly upon *Scott Paper Co.*, it is clear from the *Brulotte*

opinion, and this Court's explanation of *Brulotte* in *Aronson*, that the *Brulotte* rule of patent misuse is not the rule of *per se* invalidity which Kenner espouses.[3] *Scott Paper*, of course, did not involve a license agreement or the question of validity of a royalty term. To the extent it was applied by this Court in *Brulotte*, the language of *Scott Paper* that "any attempted reservation or continuation in the patentee . . . of the patent monopoly, after the patent expires, whatever the legal device employed, runs counter to the policy and purpose of the patent laws" (326 U.S. at 256, 66 S.Ct. 104), clearly was limited by this Court in *Brulotte* to the misuse of patent leverage, and nothing more.

The fact that the members of the American Intellectual Property Law Association have undertaken to file an amicus brief in support of this Petition for Certiorari is a strong indication of the public importance of the issue involved in this petition. To settle the confusion over what facts and circumstances require the invalidation of a royalty agreement for conflict with federal patent law; to halt the pernicious spread of a *per se* rule that permits licensees to evade payment of royalties in the name of the "public interest"; and to provide an adequate measure of certainty, for the members of the intellectual property law Bar and their clients, as to

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[3] Kenner even misquotes this Court's opinion to achieve its unwarranted conclusion. Where this Court said in *Brulotte*, "We are, therefore, unable to conjecture what the bargaining position of the parties might have been . . . had the provision for post-expiration royalties been divorced from the patent and no wise subject to its leverage," Kenner says this Court "was not interested in conjecturing" (Kenner brief page 10) and "did not want to 'conjecture' as to what the bargaining position of the parties might have been." (Kenner brief, page 22). The difference between "not interested" and "unable" is considerable. It is, as Kenner must recognize, the difference between *per se* invalidity and invalidity based upon the misuse of patent leverage.

what royalty agreements will be enforceable, this Court should grant Certiorari.

Respectfully submitted,

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No. 85-1579

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

ROBERT BOGGILD AND WILLIAM L. DALE,
Petitioners,

v.

KENNER PRODUCTS, A DIVISION OF
CPG PRODUCTS CORPORATION
Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

MOTION FOR LEAVE TO FILE AND BRIEF OF AMICUS CURIAE AMERICAN INTELLECTUAL PROPERTY LAW ASSOCIATION

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NO. 85-1579

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OCTOBER TERM, 1985

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v.

KENNER PRODUCTS, A DIVISION OF
CPG PRODUCTS CORPORATION

Respondent.

MOTION FOR LEAVE TO FILE AN

AMICUS CURIAE BRIEF

The American Intellectual Property Law Association (AIPLA) moves this Court

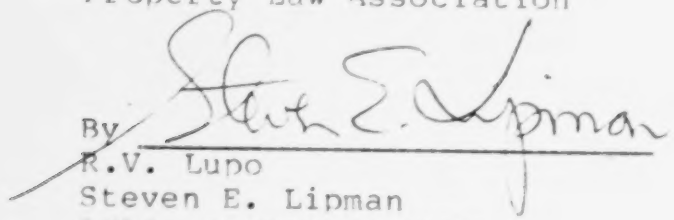
for leave to file the enclosed Brief as an Amicus Curiae in support of the request that a Writ of Certiorari be issued to review the decision and judgment of the United States Court of Appeals for the Sixth Circuit entered on November 13, 1985 and reported at 776 F.2d 1315. The AIPLA has obtained the written consent of the petitioners to file the enclosed Brief. Respondent has not given its written consent to the filing of the enclosed Brief, however, has indicated that it will not oppose the petition.

The current petition seeks review of an important area of intellectual property law which is now in a state of confusion and the AIPLA believes it

important that it present to the Court its views on the issue.

Respectfully submitted,

American Intellectual
Property Law Association

By 
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NO. 85-1579

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Respondent.

BRIEF OF AMICUS CURIAE

AMERICAN INTELLECTUAL PROPERTY

LAW ASSOCIATION

ON

PETITION FOR A WRIT OF CERTIORARI TO

THE UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

This Brief is submitted on behalf of the American Intellectual Property Law Association ("AIPLA"), as Amicus Curiae, to request that a Writ of Certiorari be issued[1/] to review the decision and judgment of the United States Court of Appeals for the Sixth Circuit entered on November 13, 1985, which reversed the decision of the United States District Court for the Southern District of Ohio, Western Division, granting summary judgment in favor of Petitioners.

1/ A "Motion For Leave to File A Brief Amicus Curiae" precedes this Brief in accordance with Rule 36.1 of this Court.

I. INTEREST OF AMICUS CURIAE

The AIPLA is a voluntary bar association of more than 5,200 attorneys interested in patent, trademark, copyright, trade secret and other laws protecting intellectual property rights. The AIPLA membership includes attorneys in private practice and attorneys employed by corporations, universities and government.

The AIPLA has no views on the private interests of the involved parties and files this Brief in the belief that certiorari should be granted because of a need for clear interpretation of the effect, if any, on a license for a term of years extending beyond the expiration date of a patent, where the license was entered into at a

time prior to either the filing of a patent application or the grant of a patent.

II. OPINIONS BELOW

This Brief adopts the Petitioners' (Boggild et al) statement of the "Opinions Below" (Petitioners' Brief at pp. 1-2).

III. JURISDICTION

This Brief adopts the Petitioners' statement of "Jurisdiction" (Petitioners' Brief at p. 2).

IV. CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

This Brief adopts the Petitioners' statement of "Constitutional Provisions

and Statutes Involved" (Petitioners' Brief at p. 2).

V. STATEMENT OF THE CASE

This Brief adopts Petitioner's "Statement Of The Case" further noting that the enumerated items of Article V of the subject license (Petitioners' Brief at p. 5) constitute what is commonly referred to in technology contracts as "technical know-how", which exists separate and apart from either a patent grant on the subject invention, or from any contemplation of the filing of a patent application on the subject invention.

VI. REASONS FOR GRANTING THE WRIT

This case presents an important question concerning the relationship between the Federal Patent Laws and the rights of the States to regulate commerce in technology that might have the potential of being subject to the Patent Laws. The Sixth Circuit's decision fails to appreciate fully this relationship and misconstrues this Court's prior precedent in Brulotte v. Thys Co., 379 U.S. 29 (1964), and Aronson v. Quick Point Pencil Company, 440 U.S. 257 (1979), in a manner contrary to the policy objectives embodied in the Constitution, Article I, Section 8, Clause 8, and in the implementing Patent Laws of Title 35, U.S. Code. The Sixth Circuit's decision

incorrectly imposes a limitation on a license for technology, particularly its agreed-to-term, to the effect that no matter what the underlying contractual consideration, the license term must end upon the expiration of any related patent, if it was in any way contemplated to file an application for patent at the time of entering into the license agreement. This Court has never so ruled.

This case presents a set of facts that clearly illustrate the error of the Sixth Circuit's ruling. In this regard, the parties entered into an agreement for a license for 25 years at a time when no patent or patent application for the subject technology existed. The agreement provided to the licensee immediate access to that technology

including substantial know-how. The licensee also received the right to make, use and sell the technology. Under these facts, without more, neither the Sixth Circuit nor the licensee has suggested that the contract was in any way illegal in providing for a twenty-five year term.

Instead, the entire basis for the Sixth Circuit's decision appears to reside in the additional fact that the parties also agreed that patent applications on the technology would be filed at a subsequent time. (Article II). The parties clearly understood that the subsequent filing of patent applications would confer no patent rights and expressly provided (at Article VI(g)) for the contingency that no patent would ever issue on those

patent applications, by providing a continuance of the royalty

> regardless of whether or not the filing of the patent applications contemplated in Article II hereof results in the issuance of a patent or patents.

Furthermore, the parties agreed (at Article XIII(d)) that the twenty-five year period would not be shortened in the event the patents did issue, by providing that the license

> ...shall run to the full end of the term or terms of any Letters Patent that may issue on or as a result of the application or applications referred to in Article II hereof, or for a period of 25 years, whichever is longer, and shall thereupon terminate.

Nevertheless, in the face of this record, the Sixth Circuit held that the parties' contemplation of the filing of

patent applications and the possible grant of patents thereon constituted "leveraging" of the patent, and hence a per se[2/] violation under this Court's precedent in Brulotte. In so doing, the Sixth Circuit also misconstrued this

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2/ It is noted that this Court has recently taken a cautious view of what constitutes a per se violation of the antitrust laws where patent "tying" agreements exist, observing that

> ...the per se label in the tying context has generated more confusion that coherent law...

Jefferson Parish Hospital District No. 2 v. Hyde, 446 U.S. 2, 104 S.Ct. 1551, 1570 (1984). Four Justices (O'Connor, Burger, Powell and Rehnquist) urged in a concurring opinion that a "rule of reason" inquiry would be more appropriate. Presumably, this Court might have a similar attitude concerning the Sixth Circuit's application of the per se rule in the context of the facts of this case.

Court's precedent in Aronson, which expressly recognizes that a license agreement may extend beyond the term of a patent, if the extended term covers the technology agreement apart from the patent rights.3/

Clearly, the practical consequences of the Sixth Circuit's interpretation of Brulotte and Aronson would be that any time private parties contract for

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3/ Implicit in the Sixth Circuit's decision is a recognition of its uncertainty in the applicability of these two cases to the instant facts:

> ...Thus, the [Supreme] Court [in Aronson] would presumably have applied Brulotte to a "hybrid" agreement embodying rights conferred under both state law and the federal patent law.

(Brulotte, 379 U.S. at 29 n. 5 (emphasis added)).

technology and a patent application is contemplated (which it virtually always is), patent leveraging has occurred and a per se violation exists if the agreed-to-time period exceeds the expiration of some yet to be defined patent.

Most fundamentally, under the facts of this case, this conclusion must be rejected. A patent application confers no legal rights whatsoever. Gayler et al v. Wilder, 51 U.S. (10 How.) 477, 13 L.Ed. 504 (1850). The application represents an "inchoate right...which ...may [be] perfect[ed]" upon issuance of the patent. Id. Indeed, a patent may never issue, or may not issue until 15 or 20 years later (e.g., the Eniac computer patent). As such, the mere contemplation of a patent application cannot, as a matter of law, constitute

patent leveraging--for, there is nothing to be leveraged. Id. Similarly, even if a patent application is not contemplated, the decision of the Sixth Circuit would impose a 17-year time limit to a license agreement if the licensor decides, after-the-fact, to file a patent application. This result is contrary to the Constitutional predicate to the Patent Laws and this Court's opinions in Brulotte and Aronson.

Further, under the facts here, after expiration of the last patent on the subject technology, the public was free to make, use and sell the technology. 35 U.S.C. §154. Only the licensee thereafter would be required to pay royalties, and such requirement was agreed to for the valuable consideration

of early access to the technology, and the transfer of technical know-how. Clearly then, the public in no way would have suffered had the Sixth Circuit upheld the license agreement.

It should be noted that an inventor has the right to forego completely Federal protection for his invention and exploit it commercially under state trade secret law. Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470 (1977). Under such a scenario, the licensor could have properly licensed the licensee, absent contemplated patent rights, for 25 (or more) years. This perspective must be maintained when considering whether the mere fact that a patent application might issue into a patent grant, should be a

per se violation under Brulotte.

Clearly, it should not.

VII. CONCLUSION

For the reasons stated, it is respectfully submitted that the petition for a writ of certiorari should be granted.

Respectfully submitted,

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